Court File No. CV-12-9539-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT,*
R.S.C. 1985 c. C-36, AS AMENDED

IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT
OF TIMMINCO LIMITED AND BÉCANCOUR SILICON INC.

Applicants

BOOK OF AUTHORITIES OF THE
RESPONDING PARTY, JOHN P. WALSH
(Stay Extension Motion returnable April 27, 2012)

Dated: April 26, 2012

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TO: **THE SERVICE LIST**

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TAB 1

Case Name:

Canwest Global Communications Corp. (Re)

**IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, C-36, as amended
AND IN THE MATTER OF a proposed plan of compromise or arrangement of Canwest Global Communications Corp. and the other applicants listed on Schedule "A"**

**[Editor's note:
Schedule A was not attached to the copy received from the Court and therefore is not included in the judgment.]**

[2009] O.J. No. 5379

61 C.B.R. (5th) 200

2009 CarswellOnt 7882

Court File No. CV-09-8241-OOCL

Ontario Superior Court of Justice
Commercial List

S.E. Pepall J.

Heard: December 8, 2009.
Judgment: December 15, 2009.

(52 paras.)

Bankruptcy and insolvency law -- Companies' Creditors Arrangement Act (CCAA) matters -- Compromises and arrangements -- Claims -- Application in this Companies' Creditors Arrangement Act matter for an order declaring that the relief sought by the "GS Parties" was subject to an Oct. 6, 2009 stay of proceedings granted -- Cross-motion by the GS Parties for an order lifting the stay so that they could pursue their motion challenging pre-filing conduct of the CMI entities, etc., dismissed -- The substance and subject matter of the motion were certainly encompassed by the stay -- The balance of convenience, the assessment of relative prejudice and the relevant merits favoured the position of the CMI Entities on the lift stay motion.

Bankruptcy and insolvency law -- Proceedings -- Practice and procedure -- Stays -- Application in this Companies' Creditors Arrangement Act matter for an order declaring that the relief sought by the "GS Parties" was subject to an Oct. 6, 2009 stay of proceedings granted -- Cross-motion by the GS Parties for an order lifting the stay so that they *could pursue their motion challenging pre-filing conduct of the CMI entities, etc., dismissed -- The substance and subject matter of the motion were certainly encompassed by the stay -- The balance of convenience, the assessment of relative prejudice and the relevant merits favoured the position of the CMI Entities on the lift stay motion.*

Application by the CCAA applicants and the "CMI entities" for an order declaring that the relief sought by the "GS parties" was subject to the stay of proceedings granted on Oct. 6, 2009. Cross-motion by GS Parties for an order lifting the stay so they could pursue their motion challenging pre-filing conduct of the CMI entities, etc. The Ad Hoc Committee of Noteholders and the Special Committee of the Board of Directors supported the position of the CMI Entities. In essence, the GS Parties' motion sought to undo the transfer of the CW Investments Co. shares from 441 to CMI or to require CMI to perform and not disclaim the shareholders agreement as though the shares had not been transferred.

HELD: GS Parties' motions dismissed, save for a portion dealing with para. 59 of the initial order on consent; CMI Entities' motion granted with the exception of a strike portion, which was moot. The first issue was caught by the stay of proceedings and the second was properly addressed if and when CMI sought to disclaim the shareholders agreement. The substance of the GS Parties' motion was a "proceeding" subject to the stay under para. 15 of the initial order prohibiting the commencement of all proceedings against or in respect of the CMI Entitites, or affecting the CMI business or property. The relief sought would also involve "the exercise of any right or remedy affecting the CMI business or the CMI property" which was stayed under para. 16 of the initial order. The substance and subject matter of the motion were certainly encompassed by the stay. The real question was whether the stay ought to be lifted in this case. If the stay were lifted, the prejudice to CMI would be great and the proceedings contemp lated by the GS Parties would be extraordinarily disruptive. The GS Parties were in no worse position than any other stakeholder who was precluded from relying on rights that arise upon an insolvency default. The balance of convenience, the assessment of relative prejudice and the relevant merits favoured the position of the CMI Entities on the lift stay motion. The onus to lift the stay was on the moving party. The stay was performing the essential function of keeping stakeholders at bay in order to give CMI Entities a reasonable opportunity to develop a restructuring plan.

Statutes, Regulations and Rules Cited:

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 32, s. 11.02

Counsel:

Lyndon Barnes, Alex Cobb and Shawn Irving for the CMI Entities.

Alan Mark and Alan Merskey for the Special Committee of the Board of Directors of Canwest.

David Byers and Maria Konyukhova for the Monitor, FTI Consulting Canada Inc.

Benjamin Zarnett and Robert Chadwick for the Ad Hoc Committee of Noteholders.

K. McElcheran and G. Gray for GS Parties.

Hugh O'Reilly and Amanda Darrach for Canwest Retirees and the Canadian Media Guild.

Hilary Clarke for Senior Secured Lenders to LP Entities.

Steve Weisz for CIT Business Credit Canada Inc.

REASONS FOR DECISION

S.E. PEPALL J.:--

Relief Requested

1 The CCAA applicants and partnerships (the "CMI Entities") request an order declaring that the relief sought by GS Capital Partners VI Fund L.P., GSCP VI AA One Holding S.ar.1 and GS VI AA One Parallel Holding S.ar.1 (the "GS Parties") is subject to the stay of proceedings granted in my Initial Order dated October 6, 2009. The GS Parties bring a cross-motion for an order that the stay be lifted so that they may pursue their motion which, among other things, challenges pre-filing conduct of the CMI Entities. The Ad Hoc Committee of Noteholders and the Special Committee of the Board of Directors support the position of the CMI Entities. All of these stakeholders are highly sophisticated. Put differently, no one is a commercial novice. Such is the context of this dispute.

Background Facts

2 Canwest's television broadcast business consists of the CTLP TV business which is comprised of 12 free-to-air television stations and a portfolio of subscription based specialty television channels on the one hand and the Specialty TV Business on the other. The latter consists of 13 specialty television channels that are operated by CMI for the account of CW Investments Co. and its subsidiaries and 4 other specialty television channels in which the CW Investments Co. ownership interest is less than 50%.

3 The Specialty TV Business was acquired jointly with Goldman Sachs from Alliance Atlantis in August, 2007. In January of that year, CMI and Goldman Sachs agreed to acquire the business of Alliance Atlantis through a jointly owned acquisition company which later became CW Investments Co. It is a Nova Scotia Unlimited Liability Corporation ("NSULC").

4 CMI held its shares in CW Investments Co. through its wholly owned subsidiary, 4414616 Canada Inc. ("441"). According to the CMI Entities, the sole purpose of 441 was to insulate CMI from any liabilities of CW Investments Co. As a NSULC, its shareholders may face exposure if the NSULC is liquidated or becomes bankrupt. As such, 441 served as a "blocker" to potential liability. The CMI Entities state that similarly the GS parties served as "blockers" for Goldman Sachs' part of the transaction.

5 According to the GS Parties, the essential elements of the deal were as follows:

(i) GS would acquire at its own expense and at its own risk, the slower growth businesses;
(ii) CW Investments Co. would acquire the Specialty TV Business and that company would be owned by 441 and the GS Parties under the terms of a Shareholders Agreement;
(iii) GS would assist CW Investments Co. in obtaining separate financing for the Specialty TV Business;
(iv) Eventually Canwest would contribute its conventional TV business on a debt free basis to CW Investments Co. in return for an increased ownership stake in CW Investments Co.

6 The GS Parties also state that but for this arrangement, Canwest had no chance of acquiring control of the Specialty TV Business. That business is subject to regulation by the CRTC. Consistent with policy objectives, the CRTC had to satisfy itself that CW Investments Co. was not controlled either at law or in fact by a non-Canadian.

7 A Shareholders Agreement was entered into by the GS parties, CMI, 441, and CW Investments Co. The GS Parties state that 441 was a critical party to this Agreement. The Agreement reflects the share ownership of each of the parties to it: 64.67% held by the GS Parties and 35.33% held by 441. It also provides for control of CW Investments Co. by distribution of voting shares: 33.33% held by the GS Parties and 66.67% held by 441. The Agreement limits certain activities of CW Investments Co. without the affirmative vote of a director nominated to its Board by the GS Parties.

The Agreement provides for call and put options that are designed to allow the GS parties to exit from the investment in CW Investments Co. in 2011, 2012, and 2013. Furthermore, in the event of an insolvency of CMI, the GS parties have the ability to effect a sale of their interest in CW Investments Co. and require as well a sale of CMI's interest. This is referred to as the drag-along provision. Specifically, Article 6.10(a) of the Shareholders Agreement states:

> Notwithstanding the other provisions of this Article 6, if an Insolvency Event occurs in respect of CanWest and is continuing, the GS Parties shall be entitled to sell all of their Shares to any *bona fide* Arm's Length third party or parties at a price and on other terms and conditions negotiated by GSCP in its discretion provided that such third party or parties acquires all of the Shares held by the CanWest Parties at the same price and on the same terms and conditions, and in such event, the CanWest Parties shall sell their Shares to such third party or parties at such price and on such terms and conditions. The Corporation and the CanWest Parties each agree to cooperate with and assist GSCP with the sale process (including by providing protected purchasers designated by GSCP with confidential information regarding the Corporation (subject to a customary confidentiality agreement) and with access to management).

8 The Agreement also provided that 441 as shareholder could transfer its CW Investments Co. shares to its parent, CMI, at any time, by gift, assignment or otherwise, whether or not for value. While another specified entity could not be dissolved, no prohibition was placed on the dissolution of 441. 441 had certain voting obligations that were to be carried out at the direction of CMI. Furthermore, CMI was responsible for ensuring the performance by 441 of its obligations under the Shareholders Agreement.

9 On October 5, 2009, pursuant to a Dissolution Agreement between 441 and CMI and as part of the winding-up and distribution of its property, 441 transferred all of its property, namely its 352,986 Class A shares and 666 Class B preferred shares of CW Investments Co., to CMI. CMI undertook to pay and discharge all of 441's liabilities and obligations. The material obligations were those contained in the Shareholders Agreement. At the time, 441 and CW Investments Co. were both solvent and CMI was insolvent. 441 was subsequently dissolved.

10 For the purposes of these two motions only, the parties have agreed that the court should assume that the transfer and dissolution of 441 was intended by CMI to provide it with the benefit of all the provisions of the CCAA proceedings in relation to contractual obligations pertaining to those shares. This would presumably include both the stay provisions found in section 11 of the CCAA and the disclaimer provisions in section 32 .

11 The CMI Entities state that CMI's interest in the Specialty TV Business is critical to the restructuring and recapitalization prospects of the CMI Entities and that if the GS parties were able to effect a sale of CW Investments Co. at this time, and on terms that suit them, it would be disastrous to the CMI Entities and their stakeholders. Even the overhanging threat of such a sale is adversely affecting the negotiation of a successful restructuring or recapitalization of the CMI Entities.

12 On October 6, 2009, I granted an Initial Order in these proceedings. CW Investments Co. was not an applicant. The CMI Entities requested a stay of proceedings to allow them to proceed to develop a plan of arrangement or compromise to implement a consensual "pre-packaged" recapitalization transaction. The CMI Entities and the Ad Hoc Committee of 8% Noteholders had agreed on terms of such a transaction that were reflected in a support agreement and term sheet. Those noteholders who support the term sheet have agreed to vote in favour of the plan subject to certain conditions one of which is a requirement that the Shareholders Agreement be amended.

13 The Initial Order included the typical stay of proceedings provisions that are found in the standard form order promulgated by the Commercial List Users Committee. Specifically, the order stated:

> 15. THIS COURT ORDERS that until and including November 5, 2009, or such later date as this Court may order (the "Stay Period"), no proceeding or enforcement process in any court or

tribunal (each, a "Proceeding") shall be commenced or continued against or in respect of the CMI Entities, the Monitor or the CMI CRA or affecting the CMI Business or the CMI Property, except with the written consent of the applicable CMI Entity, the Monitor and the CMI CRA (in respect of Proceedings affecting the CMI Entities, the CMI Property or the CMI Business), the CMI CRA (in respect of Proceedings affecting the CMI Entities, the CMI property or the CMI Business), the CMI CRA (in respect of Proceedings affecting the CMI CRA), or with leave of this Court, and any and all Proceedings currently under way against or in respect of the CMI Entities or the CMI CRA or affecting the CMI Business or the CMI Property are hereby stayed and suspended pending further Order of this Court. In the case of the CMI CRA, no Proceeding shall be commenced against the CMI CRA or its directors and officers without prior leave of this Court on seven (7) days notice to Stonecrest Capital Inc.

16. THIS COURT ORDERS that during the Stay Period, all rights and remedies of any individual, firm, corporation, governmental body or agency, or any other entities (all of the foregoing, collectively being "Persons" and each being a "Person") against or in respect of the CMI Entities, the Monitor and/or the CMI CRA, or affecting the CMI Business or the CMI Property, are hereby stayed and suspended except with the written consent of the applicable CMI Entity, the Monitor and the CMI CRA (in respect of rights and remedies affecting the CMI Entities, the CMI Property or the CMI Business), the CMI CRA (in respect of rights or remedies affecting the CMI CRA), or leave of this Court, provided that nothing in this Order shall (i) empower the CMI Entities to carry on any business which the CMI Entities are not lawfully entitled to carry on, (ii) exempt the CMI Entities from compliance with statutory or regulatory provisions relating to health, safety or the environment, (iii) prevent the filing of any registration to preserve or perfect a security interest, or (iv) prevent the registration of a claim for lien.

14 The GS parties were not given notice of the CCAA application. On November 2, 2009, they brought a motion that, among other things, seeks to set aside the transfer of the shares from 441 to CMI or, in the alternative, require CMI to perform and not disclaim the Shareholders Agreement as if the shares had not been transferred. On November 10, 2009 the GS parties purported to revive 441 by filing Articles of Revival with the Director of the CBCA. The CMI Entities were not notified nor was any leave of the court sought in this regard. In an amended notice of motion dated November 19, 2009 (the "main motion"), the GS Parties request an order:

(a) Setting aside and declaring void the transfer of the shares from 441 to CMI;
(b) declaring that the rights and remedies of the GS Parties in respect of the obligations of 441 under the Shareholders Agreement are not affected by these CCAA proceedings in any way whatsoever;
(c) in the alternative to (a) and (b), an order directing CMI to perform all of the obligations that bound 441 immediately prior to the transfer;
(d) in the alternative to (a) and (b), an order declaring that the obligations that bound 441 immediately prior to the transfer, may not be disclaimed by CMI pursuant to section 32 of the CCAA or otherwise; and
(e) if necessary, a trial of the issues arising from the foregoing.

15 They also requested an order amending paragraph 59 of the Initial Order but that issue has now been resolved and I am satisfied with the amendment proposed.

16 The CMI Entities then brought a motion on November 24, 2009 for an order that the GS motion is stayed. As in a game of chess, on December 3, 2009, the GS Parties served a cross-motion in which, if required, they seek leave to proceed with their motion.

17 In furtherance of their main motion, the GS Parties have expressed a desire to examine 4 of the 5 members of the Special Committee of the Board of Directors of Canwest. That Committee was constituted, among other things, to oversee the restructuring. The GS Parties have also demanded an extensive list of documentary production. They also seek to impose significant discovery demands upon the senior management of CanWest.

Issues

18 The issues to be determined on these motions are whether the relief requested by the GS Parties in their main motion is stayed based on the Initial Order and if so, whether the stay should be lifted. In addition, should the relief sought in paragraph 1(e) of the main motion be struck.

Positions of Parties

19 In brief, the parties' positions are as follows. The CMI Entities submit that the GS Parties' motion is a "proceeding" that is subject to the stay under paragraph 15 of the Initial Order. In addition, the relief sought by them involves "the exercise of any right or remedy affecting the CMI Business or the CMI Property" which is stayed under paragraph 16 of the Initial Order. The stay is consistent with the purpose of the CCAA. They submit that the subject matter of the motion should be caught so as to prevent the GS parties from gaining an unfair advantage over other stakeholders of the CMI Entities and to ensure that the resources of the CMI Entities are devoted to developing a viable restructuring plan for the benefit of all stakeholders. They also state that CMI's interest in CW Investments Co. is a significant portion of its enterprise value. They state further that their actions were not in breach of the Shareholders Agreement and in any event, debtor companies are able to organize their affairs in order to benefit from the CCAA stay. Furthermore, any loss suffered by the GS Parties can be quantified.

20 In paragraph 1(e) of the main motion, the GS parties seek to prevent CMI from disclaiming the obligations of 441 that existed immediately prior to the transfer of the shares to CMI. If this relief is not stayed, the CMI Entities submit that it should be struck out pursuant to Rule 25.11(b) and (c) as premature and improper. They also argue that section 32 of the CCAA provides a procedure for disclaimer of agreements which the GS Parties improperly seek to circumvent.

21 Lastly, the CMI Entities state that the bases on which a CCAA stay should be lifted are very limited. Most of the grounds set forth in *Re Canadian Airlines Corp.*[1] which support the lifting of a stay are manifestly inapplicable. As to prejudice, the GS parties are in no worse position than any other stakeholder who is precluded from relying on rights that arise on an insolvency default. In contrast, the prejudice to the CMI Entities would be debilitating and their resources need to be devoted to their restructuring. The GS Parties' rights would not be lost by the passage of time. The GS Parties' motion is all about leverage and a desire to improve the GS Parties' negotiating position submits counsel for the CMI Entities.

22 The Ad Hoc Committee of Noteholders, as mentioned, supports the CMI Entities' position. In examining the context of the dispute, they submit that the Shareholders Agreement permitted and did not prohibit the transfer of 441's shares. Furthermore, the operative obligations in that agreement are obligations of CMI, not 441. It is the substance of the GS Parties' claims and not the form that should govern their ability to pursue them and it is clearly encompassed by the stay. The Committee relies on *Chef Ready Foods Ltd. v. Hongkong Bank of Canada*[2] in support of their position on timing.

23 The Special Committee also supports the CMI Entities. It submits that the primary relief sought by the GS parties is a declaration that their contracts to and with CW Investments cannot or should not be disclaimed. The debate as to whether 441 could properly be assimilated into CMI is no more than an alternate argument as to why such disclaimer can or cannot occur. They state that the subject matter of the GS Parties' motion is premature.

24 The GS Parties submit that the stay does not prevent parties affected by the CCAA proceedings from bringing motions within the CCAA proceedings themselves. The use of CCAA powers and the scope of the stay provided in the Initial Order and whether it applies to the GS Parties' motion are proper questions for the court charged with supervising the CCAA process. They also argue that the motion would facilitate negotiation between key parties, raises the important preliminary issue of the proper scope and application of section 32 of the CCAA, and avoids putting the

Monitor in the impossible position of having to draw legal conclusions as to the scope of CMI's power to disclaim. The court should be concerned with pre-filing conduct including the reason for the share transfer, the timing, and CMI's intentions.

25 Even if the stay is applicable, the GS parties submit that it should be lifted. In this regard, the court should consider the balance of convenience, the relative prejudice to parties, and where relevant, the merits of the proposed action. The court should also consider whether the debtor company has acted and is acting in good faith. The GS Parties were the medium by which the Specialty TV Business became part of Canwest. Here, all that is being sought is a reversal of the false and highly prejudicial start to these restructuring proceedings. It is necessary to take steps now to protect a right that could be lost by the passage of time. The transfer of the shares exhibited bad faith on the part of Canwest. 441 insulated CW Investments Co. and the Specialty TV Business from the insolvency of CMI and thereby protected the contractual rights of the GS Parties. The manifest harm to the GS Parties that invited the motion should be given weight in the court's balancing of prejudices. Concerns as to disruption of the restructuring process could be met by imposing conditions on the lifting of a stay as, for example, the establishment of a timetable.

Discussion

(a) Legal Principles

26 First I will address the legal principles applicable to the granting and lifting of a CCAA stay.

27 The stay provisions in the CCAA are discretionary and are extraordinarily broad. Section 11.02 (1) and (2) states:

> 11.02 (1) A court may, on an initial application in respect of a debtor company, make an order on any terms that it may impose, effective for the period that the court considers necessary, which period may not be more than 30 days,
>
> (a) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under the Bankruptcy and Insolvency Act or the Winding-up and Restructuring Act;
> (b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and
> (c) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.
> (2) A court may, on an application in respect of a debtor company other than an initial application, make an order, on any terms that it may impose,
> (a) staying until otherwise ordered by the court, for any period that the court considers necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in paragraph (1)(a);
> (b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and
> (c) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

28 The underlying purpose of the court's power to stay proceedings has frequently been described in the case law. It is the engine that drives the broad and flexible statutory scheme of the CCAA: *Re Stelco Inc*[3] and the key element of the CCAA process: *Re Canadian Airlines Corp.*[4] The power to grant the stay is to be interpreted broadly in order to permit the CCAA to accomplish its legislative purpose. As noted in *Re Lehndorff General Partner Ltd.*[5], the power to grant a stay extends to effect the position of a company's secured and unsecured creditors as well as other parties who could potentially jeopardize the success of the restructuring plan and the continuance of the company. As stated by Farley J. in that case,

> "It has been held that the intention of the CCAA is to prevent any manoeuvres for positioning among the creditors during the period required to develop a plan and obtain approval of creditors. Such manoeuvres could give an aggressive creditor an advantage to the prejudice of others who are less aggressive and would undermine the company's financial position making it even less likely that the plan will succeed. ... The possibility that one or more creditors may be prejudiced should not affect the court's exercise of its authority to grant a stay of proceedings under the CCAA because this affect is offset by the benefit to all creditors and to the company of facilitating a reorganization. The court's primary concerns under the CCAA must be for the debtor and *all* of the creditors."[6] (Citations omitted)

29 The all encompassing scope of the CCAA is underscored by section 8 of the Act which precludes parties from contracting out of the statute. See *Chef Ready Foods Ltd. v. Hongkong Bank of Canada*[7] in this regard.

30 Two cases dealing with stays merit specific attention. *Campeau v. Olympia & York Developments Ltd.*[8] was a decision granted in the early stages of the evolution of the CCAA. In that case, the plaintiffs brought an action for damages including the loss of share value and loss of opportunity both against a company under CCAA protection and a bank. The statement of claim had been served before the company's CCAA filing. The plaintiff sought to lift the stay to proceed with its action. The bank sought an order staying the action against it pending the disposition of the CCAA proceedings. Blair J. examined the stay power described in the CCAA, section 106 of the Courts of Justice Act[9] and the court's inherent jurisdiction. He refused to lift the stay and granted the stay in favour of the bank until the expiration of the CCAA stay period. Blair J. stated that the plaintiff's claims may be addressed more expeditiously in the CCAA proceeding itself.[10] Presumably this meant through a claims process and a compromise of claims. The CCAA stay precludes the litigating of claims comparable to the plaintiff's in *Campeau*. If it were otherwise, the stay would have no meaningful impact.

31 The decision of *Chef Ready Foods Ltd. v. Hongkong Bank of Canada* is also germane to the case before me. There, the Bank demanded payment from the debtor company and thereafter the debtor company issued instant trust deeds to qualify for protection under the CCAA. The bank commenced proceedings on debenture security and the next day the company sought relief under the CCAA. The court stayed the bank's enforcement proceedings. The bank appealed the order and asked the appellate court to set aside the stay order insofar as it restrained the bank from exercising its rights under its security. The B.C. Court of Appeal refused to do so having regard to the broad public policy objectives of the CCAA.

32 As with the imposition of a stay, the lifting of a stay is discretionary. There are no statutory guidelines contained in the Act. According to Professor R.H. McLaren in his book "Canadian Commercial Reorganization: Preventing Bankruptcy"[11], an opposing party faces a very heavy onus if it wishes to apply to the court for an order lifting the stay. In determining whether to lift the stay, the court should consider whether there are sound reasons for doing so consistent with the objectives of the CCAA, including a consideration of the balance of convenience, the relative prejudice to parties, and where relevant, the merits of the proposed action: *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.*[12]. That decision also indicated that the judge should consider the good faith and due diligence of the debtor company.[13]

33 Professor McLaren enumerates situations in which courts will lift a stay order. The first six were cited by Paperny J. in 2000 in *Re Canadian Airlines Corp.*[14] and Professor McLaren has added three more since then. They are:

1. When the plan is likely to fail.
2. The applicant shows hardship (the hardship must be caused by the stay itself and be independent of any pre-existing condition of the applicant creditor).
3. The applicant shows necessity for payment (where the creditors' financial problems are created

by the order or where the failure to pay the creditor would cause it to close and thus jeopardize the debtor's company's existence).

4. The applicant would be significantly prejudiced by refusal to lift the stay and there would be no resulting prejudice to the debtor company or the positions of creditors.
5. It is necessary to permit the applicant to take steps to protect a right which could be lost by the passing of time.
6. After the lapse of a significant time period, the insolvent is no closer to a proposal than at the commencement of the stay period.
7. There is a real risk that a creditor's loan will become unsecured during the stay period.
8. It is necessary to allow the applicant to perfect a right that existed prior to the commencement of the stay period.
9. It is in the interests of justice to do so.

(b) Application

34 Turning then to an application of all of these legal principles to the facts of the case before me, I will first consider whether the subject matter of the main motion of the GS Parties is captured by the stay and then will address whether the stay should be lifted.

35 In analyzing the applicability of the stay, I must examine the substance of the main motion of the GS Parties and the language of the stay found in paragraphs 15 and 16 of my Initial Order.

36 In essence, the GS Parties' motion seeks to:

(i) undo the transfer of the CW Investments Co. shares from 441 to CMI or
(ii) require CMI to perform and not disclaim the Shareholders Agreement as though the shares had not been transferred.

37 It seems to me that the first issue is caught by the stay of proceedings and the second issue is properly addressed if and when CMI seeks to disclaim the Shareholders Agreement.

38 The substance of the GS Parties' motion is a "proceeding" that is subject to the stay under paragraph 15 of the Initial Order which prohibits the commencement of all proceedings against or in respect of the CMI Entities, or affecting the CMI Business or the CMI Property. The relief sought would also involve "the exercise of any right or remedy affecting the CMI Business or the CMI Property" which is stayed under paragraph 16 of the Initial Order.

39 When one examines the relief requested in detail, the application of the stay is clear. The GS Parties ask first for an order setting aside and declaring void the transfer of the shares from 441. As the shares have been transferred to the CMI Entities presumably pursuant to section 6.5(a) of the Shareholders Agreement, this is relief "affecting the CMI Property". Secondly, the GS Parties ask for a declaration that the rights and remedies of the GS Parties in respect of the obligations of 441 are not affected by the CCAA proceedings. This relief would permit the GS Parties to require CMI to tender the shares for sale pursuant to section 6.10 of the Shareholders Agreement. This too is relief affecting the CMI Entities and the CMI Property. Thirdly, they ask for an order directing CMI to perform all of the obligations that bound 441 prior to the transfer. This represents the exercise of a right or remedy against CMI and would affect the CMI Business and CMI Property in violation of paragraph 16 of the Initial Order. This is also stayed by virtue of paragraph 15. Fourthly, the GS Parties seek an order declaring that the obligations that bound 441 prior to the transfer may not be disclaimed. This both violates paragraph 16 of the Initial Order and also seeks to avoid the express provisions contained in the recent amendments to the CCAA that address disclaimer.

40 Accordingly, the substance and subject matter of the GS Parties' motion are certainly encompassed by the stay. As Mr. Barnes for the CMI Entities submitted, had CMI taken the steps it did six months ago and the GS Parties commenced a lawsuit, the action would have been stayed. Certainly to the extent that the GS Parties are seeking the freedom to exercise their drag along rights, these rights should be captured by the stay.

41 The real question, it seems to me, is whether the stay should be lifted in this case. In considering the request to lift the stay, it is helpful to consider the context and the provisions of the Shareholders Agreement. In his affidavit sworn November 24, 2009, Mr. Strike, the President of Corporate Development & Strategy Implementation of Canwest Global and its Recapitalization Officer, states that the joint acquisition from Alliance Atlantis was intensely and very carefully negotiated by the parties and that the negotiation was extremely complex and difficult. "Every aspect of the deal was carefully scrutinized, including the form, substance and precise terms of the Initial Shareholders Agreement." The Shareholders Agreement was finalized following the CRTC approval hearing. Among other things:

- Article 2.2 (b) provides that CMI is responsible for ensuring the performance by 441 of its obligations under the Shareholders Agreement.
- Article 6.1 contains a restriction on the transfer of shares.
- Article 6.5 addresses permitted transfers. Subsection (a) expressly permits each shareholder to transfer shares to a parent of the shareholder. CMI was the parent of the shareholder, 441.
- Article 6.10 provides that notwithstanding the other provisions of Article 6, if an insolvency event occurs (which includes the commencement of a CCAA proceeding), the GS Parties may sell their shares and cause the Canwest parties to sell their shares on the same terms. This is the drag along provision.
- Article 6.13 prohibits the liquidation or dissolution of another company[15] without the prior written consent of one of the GS Parties[16].

42 The recital of these provisions and the absence of any prohibition against the dissolution of 441 indicate that there is a good arguable case that the Shareholders Agreement, which would inform the reasonable expectations of the parties, permitted the transfer and dissolution.

43 The GS Parties are in no worse position than any other stakeholder who is precluded from relying on rights that arise upon an insolvency default. As stated in *San Francisco Gifts Ltd.*[17]:

> "The Initial Order enjoined all of San Francisco's landlords from enforcing contractual insolvency clauses. This is a common prohibition designed, at least in part, to avoid a creditor frustrating the restructuring by relying on a contractual breach occasioned by the very insolvency that gave rise to proceedings in the first place."[18]

44 Similarly, in *Norcen Energy Resources Ltd.*[19], one of the debtor's joint venture partners in certain petroleum operations was unable to rely on an insolvency clause in an agreement that provided for the immediate replacement of the operator if it became bankrupt or insolvent.

45 If the stay were lifted, the prejudice to CMI would be great and the proceedings contemplated by the GS Parties would be extraordinarily disruptive. The GS Parties have asked to examine 4 of the 5 members of the Special Committee. The Special Committee is a committee of the Board of Directors of Canwest. Its mandate includes, among other things, responsibility for overseeing the implementation of a restructuring with respect to all, or part of the business and/or capital structure of Canwest. The GS Parties have also requested an extensive list of documentary production including all documents considered by the Special Committee and any member of that Committee relating to the matters at issue; all documents considered by the Board of Directors and any member of the Board of Directors relating to the matters at issue; all documents evidencing the deliberations, discussions and decisions of the Special Committee and the Board of Directors relating to the matters at issue; all documents relating to the matters at issue sent to or received by Leonard Asper, Derek Burney, David Drybrough, David Kerr, Richard Leipsic, John Maguire, Margot Micillef, Thomas Strike, and Hap Stephen, the Chief Restructuring Advisor appointed by the court. As stated by Mr.

Strike in his affidavit sworn November 24, 2009,

> "The witnesses that the GS Parties propose to examine include the most senior executives of the CMI Entities; those who are most intensely involved in the enormously complex process of achieving a successful going concern restructuring or recapitalization of the CMI Entities. Myself, Mr. Stephen, Mr. Maguire and the others are all working flat out on trying to achieve a successful restructuring or recapitalization of the CMI Entities. Frankly, the last thing we should be doing at this point is preparing for a forensic examination, in minute detail, over events that have taken place over the past several months. At this point in the restructuring/recapitalization process, the proposed examination would be an enormous distraction and would significantly prejudice the CMI Entities' restructuring and recapitalization efforts."

46 While Mr. McElcheran for the GS Parties submits that the examinations and the scope of the examinations could be managed, in my view, the litigating of the subject matter of the motion would undermine the objective of protecting the CMI Entities while they attempt to restructure. The GS Parties continue to own their shares in CW Investments Co. as does CMI. CMI continues to operate the Specialty TV Business. Furthermore, CMI cannot sell the shares without the involvement of the Monitor and the court. None of these facts have changed. The drag along rights are stayed (although as Mr. McElcheran said, it is the cancellation of those rights that the GS Parties are concerned about.)

47 A key issue will be whether the CMI Parties can then disclaim that Agreement or whether they should be required to perform the obligations which previously bound 441. This issue will no doubt arise if and when the CMI Entities seek to disclaim the Shareholders Agreement. It is premature to address that issue now. Furthermore, section 32 of the CCAA now provides a detailed process for disclaimer. It states:

> 32.(1) Subject to subsections (2) and (3), a debtor company may -- on notice given in the prescribed form and manner to the other parties to the agreement and the monitor -- disclaim or resiliate any agreement to which the company is a party on the day on which proceedings commence under this Act. The company may not give notice unless the monitor approves the proposed disclaimer or resiliation.
>
> (2) Within 15 days after the day on which the company gives notice under subsection (1), a party to the agreement may, on notice to the other parties to the agreement and the monitor, apply to a court for an order that the agreement is not to be disclaimed or resiliated.
>
> (3) If the monitor does not approve the proposed disclaimer or resiliation, the company may, on notice to the other parties to the agreement and the monitor, apply to a court for an order that the agreement be disclaimed or resiliated.
>
> (4) In deciding whether to make the order, the court is to consider, among other things,
>
> (a) whether the monitor approved the proposed disclaimer or resiliation;
>
> (b) whether the disclaimer or resiliation would enhance the prospects of a viable compromise or arrangement being made in respect of the company; and
>
> (c) whether the disclaimer or resiliation would likely cause significant financial hardship to a party to the agreement.

48 Section 32, therefore, provides the scheme and machinery for the disclaimer of an agreement. If the monitor approves the disclaimer, another party may contest it. If the monitor does not approve the disclaimer, permission of the court must be obtained. It seems to me that the issues surrounding any attempt at disclaimer in this case should be canvassed on the basis mandated by Parliament in section 32 of the amended Act.

49 In my view, the balance of convenience, the assessment of relative prejudice and the relevant merits favour the position of the CMI Entities on this lift stay motion. As to the issue of good faith, the question is whether, absent more, one can infer a lack of good faith based on the facts outlined in the materials filed including the agreed upon admission by the CMI Entities. The onus to lift the stay is on the moving party. I decline to exercise my discretion to lift the stay on this basis.

50 Turning then to the factors listed by Professor McLaren, again I am not persuaded that based on the current state of affairs, any of the factors are such that the stay should be lifted. In light of this determination, there is no need to address the motion to strike paragraph 1(e) of the GS Parties' main motion.

51 The stay of proceedings in this case is performing the essential function of keeping stakeholders at bay in order to give the CMI Entities a reasonable opportunity to develop a restructuring plan. The motions of the GS Parties are dismissed (with the exception of that portion dealing with paragraph 59 of the Initial Order which is on consent) and the motion of the CMI Entities is granted with the exception of the strike portion which is moot.

52 The Monitor, reasonably in my view, did not take a position on these motions. Its counsel, Mr. Byers, advised the court that the Monitor was of the view that a commercial resolution was the best way to resolve the GS Parties' issues. It is difficult to disagree with that assessment.

S.E. PEPALL J.

cp/e/qlrds/qljxr/qlced/qlaxw/qlcas

1 (2000), 19 C.B.R. (4th) 1.

2 [1990] B.C.J. No. 2384 (C.A.) at p. 4.

3 (2005), 75 O.R. (3d) 5 (C.A.) at para. 36.

4 (2000), 19 C.B.R. (4th) 1.

5 (1993), 17 C.B.R. (3d) 24.

6 Ibid, at p. 32.

7 Supra, note 2

8 (1992) 14 C.B.R. (3d) 303.

9 R.S.O. 1990, c. C.43.

10 Supra, note 6 at paras. 24 and 25.

11 (Aurora: Canada Law Book, looseleaf) at para. 3.3400.

12 (2007), 33 C.B.R. (5th) 50 (Sask. C.A.) at para. 68.

13 Ibid, at para. 68.

14 Supra, note 3.

15 This was 4414641 Canada Inc. but not 4414616 Canada Inc., the company in issue before me.

16 Specifically, GS Capital Partners VI Fund, L.P.

17 5 C.B.R. (5th) 92 at para. 37.

18 Ibid, at para. 37.

19 (1988), 72 C.B.R. (N.S.) 1.

TAB 2

CITATION: Nelson Financial Group Ltd., 2010 ONSC 6229
COURT FILE NO.: 10-8630-00CL
DATE: 20101116

ONTARIO

SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

IN THE MATTER OF THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, C-36, AS AMENDED

AND IN THE MATTER OFA PLAN OF COMPROMISE OR ARRANGEMENT OF NELSON FINANCIAL GROUP LTD.

COUNSEL: *Richard B. Jones and Douglas Turner, Q.C.* Representative Counsel for Noteholders/Moving Party
J.H. Grout and S. Aggarwal for the Monitor
Pamela Foy for the Ontario Securities Commission
Frank Lamie for Nelson Financial Group Ltd.
Robert Benjamin Mills and Harold Van Winssen for Clifford Styles, Jackie Styles and Play Investments Ltd., Respondents
Michael Beardsley, Self Represented Respondent
Clifford Holland, Self Represented Respondent
Arnold Bolliger, Self Represented Respondent
John McVey, Self Represented Respondent
Joan Frederick, Self Represented Respondent
Rakesh Sharma, Self Represented Respondent
Larry Debono, Self Represented Respondent
Keith McClear, Self Represented Respondent

REASONS FOR DECISION

PEPALL J.

[1] This motion addresses the legal characterization of claims of holders of preferred shares in the capital stock of the applicant, Nelson Financial Group Ltd. ("Nelson"). The issue before me is to determine whether such claims constitute equity claims for the purposes of sections 6(8) and 22.1 of the *Companies' Creditors Arrangement Act* ("*CCAA*").

Background Facts

[2] Nelson was incorporated pursuant to the *Business Corporations Act* of Ontario in September, 1990. Nelson raised money from investors and then used those funds to extend credit to customers in vendor assisted financing programmes. It raised money in two ways. It issued promissory notes bearing a rate of return of 12% per annum and also issued preference shares typically with an annual dividend of 10%.[1] The funds were then lent out at significantly higher rates of interest.

[3] The Monitor reported that Nelson placed ads in selected publications. The ads outlined the nature of the various investment options. Term sheets for the promissory notes or the preferred shares were then provided to the investors by Nelson together with an outline of the proposed tax treatment for the investment. No funds have been raised from investors since January 29, 2010.

(a) Noteholders

[4] As of the date of the *CCAA* filing on March 23, 2010, Nelson had issued 685 promissory notes in the aggregate principal amount of $36,583,422.89. The notes are held by approximately 321 people.

[1] The Monitor is aware of six preferred shareholders with dividends that ranged from 10.5% to 13.75% per annum.

(b) Preferred Shareholders

[5] Nelson was authorized to issue two classes of common shares and 2,800,000 Series A preferred shares and 2,000,000 Series B preferred shares, each with a stated capital of $25.00. The president and sole director of Nelson, Marc Boutet, is the owner of all of the issued and outstanding common shares. By July 31, 2007, Nelson had issued to investors 176,675 Series A preferred shares for an aggregate consideration of $4,416,925. During the subsequent fiscal year ended July 31, 2008, Nelson issued a further 172,545 Series A preferred shares and 27,080 Series B preferred shares. These shares were issued for an aggregate consideration of $4,672,383 net of share issue costs.

[6] The preferred shares are non-voting and take priority over the common shares. The company's articles of amendment provide that the preferred shareholders are entitled to receive fixed preferential cumulative cash dividends at the rate of 10% per annum. Nelson had the unilateral right to redeem the shares on payment of the purchase price plus accrued dividends. At least one investor negotiated a right of redemption. Two redemption requests were outstanding as of the *CCAA* filing date.

[7] As of the *CCAA* filing date of March 23, 2010, Nelson had issued and outstanding 585,916.6 Series A and Series B preferred shares with an aggregate stated capital of $14,647,914. The preferred shares are held by approximately 82 people. As of the date of filing of these *CCAA* proceedings, there were approximately $53,632 of declared but unpaid dividends outstanding with respect to the preferred shares and $73,652.51 of accumulated dividends.

[8] Investors subscribing for preferred shares entered into subscription agreements described as term sheets. These were executed by the investor and by Nelson. Nelson issued share certificates to the investors and maintained a share register recording the name of each preferred shareholder and the number of shares held by each shareholder.

[9] As reported by the Monitor, notwithstanding that Nelson issued two different series of preferred shares, the principal terms of the term sheets signed by the investors were almost identical and generally provided as follows:

- the issuer was Nelson;
- the par value was fixed at $25.00;
- the purpose was to finance Nelson's business operations;
- the dividend was 10% per annum, payable monthly, commencing one month after the investment was made;
- preferred shareholders were eligible for a dividend tax credit;
- Nelson issued annual T-3 slips on account of dividend income to the preferred shareholders;
- the preferred shares were non-voting (except where voting as a class was required), redeemable at the option of Nelson and ranked ahead of common shares; and
- dividends were cumulative and no dividends were to be paid on common shares if preferred share dividends were in arrears.

[10] In addition, the Series B term sheet provided that the monthly dividend could be reinvested pursuant to a Dividend Reinvestment Plan ("DRIP").

[11] The preferred shareholders were entered on the share register and received share certificates. They were treated as equity in the company's financial statements. Dividends were received by the preferred shareholders and they took the benefit of the advantageous tax treatment.

(c) Insolvency

[12] Mr. Boutet knew that Nelson was insolvent since at least its financial year ended July 31, 2007. Nelson did not provide financial statements to any of the preferred shareholders prior to, or subsequent to, the making of the investment.

(d) Ontario Securities Commission

[13] On May 12, 2010, the Ontario Securities Commission ("OSC") issued a Notice of Hearing and Statement of Allegations alleging that Nelson and its affiliate, Nelson Investment Group Ltd., and various officers and directors of those corporations committed breaches of the *Ontario Securities Act* in the course of selling preferred shares. The allegations include non-compliance with the prospectus requirements, the sale of shares in reliance upon exemptions that were inapplicable, the sale of shares to persons who were not accredited investors, and fraudulent and negligent misrepresentations made in the course of the sale of shares. The OSC hearing has been scheduled for the end of February, 2011.

(e) Legal Opinion

[14] Based on the Monitor's review, the preferred shareholders were documented as equity on Nelson's books and records and financial statements. Pursuant to court order, the Monitor

retained Stikeman Elliott LLP as independent counsel to provide an opinion on the characterization of the claims and potential claims of the preferred shareholders. The opinion concluded that the claims were equity claims. The Monitor posted the opinion on its website and also advised the preferred shareholders of the opinion and conclusions by letter. The opinion was not to constitute evidence, issue estoppel or res judicata with respect to any matters of fact or law referred to therein. The opinion, at least in part, informed Nelson's position which was supported by the Monitor, that independent counsel for the preferred shareholders was unwarranted in the circumstances.

(f) Development of Plan

[15] The Monitor reported in its Eighth Report that a plan is in the process of being developed and that preferred shareholders would have their existing preference shares cancelled and would then be able to claim a tax loss on their investment or be given a new form of preference shares with rights to be determined.

Motion

[16] The holders of promissory notes are represented by Representative Counsel appointed pursuant to my order of June 15, 2010. Representative Counsel wishes to have some clarity as to the characterization of the preferred shareholders' claims. Accordingly, Representative Counsel has brought a motion for an order that all claims and potential claims of the preferred shareholders against Nelson be classified as equity claims within the meaning of the *CCAA*. In addition, Representative Counsel requests that the unsecured creditors, which include the noteholders, be entitled to be paid in full before any claim of a preferred shareholder and that the

preferred shareholders form a separate class that is not entitled to vote at any meeting of creditors. Nelson and the Monitor support the position of Representative Counsel. The OSC is unopposed.

[17] On the return of the motion, some preferred shareholders were represented by counsel from Templeman Menninga LLP and some were self-represented. It was agreed that the letters and affidavits of preferred shareholders that were filed with the court would constitute their evidence. Oral submissions were made by legal counsel and by approximately eight individuals. They had many complaints. Their allegations against Nelson and Mr. Boutet range from theft, fraud, misrepresentation including promises that their funds would be secured, operation of a Ponzi scheme, breach of trust, dividend payments to some that exceeded the rate set forth in Nelson's articles, conversion of notes into preferred shares at a time when Nelson was insolvent, non-disclosure, absence of a prospectus or offering memorandum disclosure, oppression, violation of section 23(3) of the *OBCA* and of the *Securities Act* such that the issuance of the preferred shares was a nullity, and breach of fiduciary duties.

[18] The stories described by the investors are most unfortunate. Many are seniors and pensioners who have invested their savings with Nelson. Some investors had notes that were rolled over and replaced with preference shares. Mr. McVey alleges that he made an original promissory note investment which was then converted arbitrarily and without his knowledge into preference shares. He alleges that the documents effecting the conversion did not contain his authentic signature.

[19] Mr. Styles states that he and his company invested approximately $4.5 million in Nelson. He states that Mr. Boutet persuaded him to convert his promissory notes into preference shares by promising a 13.75% dividend rate, assuring him that the obligation of Nelson to repay would be treated the same or better than the promissory notes, and that they would have the same or a priority position to the promissory notes. He then received dividends at the 13.75% rate contrary to the 10% rate found in the company's articles. In addition, at the time of the conversion, Nelson was insolvent.

[20] In brief, Mr. Styles submits that:

(a) the investment transactions were void because there was no prospectus contrary to the provisions of the *Securities Act* and the Styles were not accredited investors; the preferred shares were issued contrary to section 23(3) of the *OBCA* in that Nelson was insolvent at the relevant time and as such, the issuance was a nullity; and the conduct of the company and its principal was oppressive contrary to section 248 of the *OBCA*; and that

(b) the Styles' claim is in respect of an undisputed agreement relating to the conversion of their promissory notes into preferred shares which agreement is enforceable separate and apart from any claim relating to the preferred shares.

<u>The Issue</u>

[21] Are any of the claims advanced by the preferred shareholders equity claims within section 2 of the *CCAA* such that they are to be placed in a separate class and are subordinated to the full recovery of all other creditors?

The Law

[22] The relevant provisions of the *CCAA* are as follows.

Section 2 of the *CCAA* states:

> In this Act,
>
> "Claim" means any indebtedness, liability or obligation of any kind that would be a claim provable within the meaning of section 2 of the *Bankruptcy and Insolvency Act*;
>
> "Equity Claim" means a claim that is in respect of an equity interest, including a claim for, among others,
>
> (a) a dividend or similar payment,
>
> (b) a return of capital,
>
> (c) a redemption or retraction obligation,
>
> (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or
>
> (e) contribution or indemnity in respect of a claim referred to in any of paragraphs (*a*) to (*d*);"
>
> "Equity Interest" means
>
> (a) in the case of a corporation other than an income trust, a share in the corporation — or a warrant or option or another right to acquire a share in the corporation — other than one that is derived from a convertible debt, and
>
> (b) in the case of an income trust, a unit in the income trust — or a warrant or option or another right to acquire a unit in the income trust — other than one that is derived from a convertible debt;

Section 6(8) states:

> No compromise or arrangement that provides for the payment of an equity claim is to be sanctioned by the court unless it provides that all claims that are not equity claims are to be paid in full before the equity claim is to be paid.

Section 22.1 states:

> Despite subsection 22(1) creditors having equity claims are to be in the same class of creditors in relation to those claims unless the court orders otherwise and may not, as members of that class, vote at any meeting unless the court orders otherwise.

[23] Section 2 of the *Bankruptcy and Insolvency Act* ("*BIA*") which is referenced in section 2 of the *CCAA* provides that a claim provable includes any claim or liability provable in proceedings under the Act by a creditor. Creditor is then defined as a person having a claim provable as a claim under the Act.

[24] Section 121(1) of the *BIA* describes claims provable. It states:

> All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which the bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act.

[25] Historically, the claims and rights of shareholders were not treated as provable claims and ranked after creditors of an insolvent corporation in a liquidation. As noted by Laskin J.A. in *Re Central Capital Corporation*[2], on the insolvency of a company, the claims of creditors have always ranked ahead of the claims of shareholders for the return of their capital. This

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[2] (1996), 38 C.B.R. (3d) 1 (Ont. C.A.).

principle is premised on the notion that shareholders are understood to be higher risk participants who have chosen to tie their investment to the fortunes of the corporation. In contrast, creditors choose a lower level of exposure, the assumption being that they will rank ahead of shareholders in an insolvency. Put differently, amongst other things, equity investors bear the risk relating to the integrity and character of management.

[26] This treatment also has been held to encompass fraudulent misrepresentation claims advanced by a shareholder seeking to recover his investment: *Re Blue Range Resource Corp.*[3] In that case, Romaine J. held that the alleged loss derived from and was inextricably intertwined with the shareholder interest. Similarly, in the United States, the Second Circuit Court of Appeal in *Re Stirling Homex Corp.*[4] concluded that shareholders, including those who had allegedly been defrauded, were subordinate to the general creditors when the company was insolvent. The Court stated that "the real party against which [the shareholders] are seeking relief is the body of general creditors of their corporation. Whatever relief may be granted to them in this case will reduce the percentage which the general creditors will ultimately realize upon their claims." *National Bank of Canada v. Merit Energy Ltd.*[5] and *Earthfirst Canada Inc.*[6] both treated claims relating to agreements that were collateral to equity claims as equity claims. These cases dealt

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[3] 2000, 15 C.B.R. (4th) 169.

[4] (1978) 579 F. 2d 206 (2nd Cir. Ct. of App.).

[5] (2001), 2001 CarswellAlta. 913, aff'd 2002 CarswellAlta 23 (Alta C.A.).

[6] (2009) 2009 CarswellAlta 1069.

with separate indemnification agreements and the issuance of flow through shares. The separate agreements and the ensuing claims were treated as part of one integrated transaction in respect of an equity interest. The case law has also recognized the complications and delay that would ensue if *CCAA* proceedings were mired in shareholder claims.

[27] The amendments to the *CCAA* came into force on September 18, 2009. It is clear that the amendments incorporated the historical treatment of equity claims. The language of section 2 is clear and broad. Equity claim means a claim in respect of an equity interest and includes, amongst other things, a claim for rescission of a purchase or sale of an equity interest. Pursuant to sections 6(8) and 22.1, equity claims are rendered subordinate to those of creditors.

[28] The Nelson filing took place after the amendments and therefore the new provisions apply to this case. Therefore, if the claims of the preferred shareholders are properly characterized as equity claims, the relief requested by Representative Counsel in his notice of motion should be granted.

[29] Guidance on the appropriate approach to the issue of characterization was provided by the Ontario Court of Appeal in *Re Central Capital Corporation*[7]. Central Capital was insolvent and sought protection pursuant to the provisions of the *CCAA*. The appellants held preferred shares of Central Capital. The shares each contained a right of retraction, that is, a right to require Central Capital to redeem the shares on a fixed date and for a fixed price. One

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[7] Supra, note 2.

shareholder exercised his right of retraction and the other shareholder did not but both filed proofs of claim in the *CCAA* proceedings. In considering whether the two shareholders had provable debt claims, Laskin J.A. considered the substance of the relationship between the company and the shareholders. If the governing instrument contained features of both debt and equity, that is, it was hybrid in character, the court must determine the substance of the relationship between the company and the holder of the certificate. The Court examined the parties' intentions.

[30] In *Central Capital*, Laskin J.A. looked to the share purchase agreements, the conditions attaching to the shares, the articles of incorporation and the treatment given to the shares in the company's financial statements to ascertain the parties' intentions and determined that the claims were equity and not debt claims.

[31] In this case, there are characteristics that are suggestive of a debt claim and of an equity claim. That said, in my view, the preferred shareholders are, as their description implies, shareholders of Nelson and not creditors. In this regard, I note the following.

(a) Investors were given the option of investing in promissory notes or preference shares and opted to invest in shares. Had they taken promissory notes, they obviously would have been creditors. The preference shares carried many attractions including income tax advantages.

(b) The investors had the right to receive dividends, a well recognized right of a shareholder.

(c) The preference share conditions provided that on a liquidation, dissolution or winding up, the preferred shareholders ranked ahead of common shareholders. As in *Central Capital*, it is implicit that they therefore would rank behind creditors.

(d) Although I acknowledge that the preferred shareholders did not receive copies of the financial statements, nonetheless, the shares were treated as equity in Nelson's financial statements and in its books and records.

[32] The substance of the arrangement between the preferred shareholders and Nelson was a relationship based on equity and not debt. Having said that, as I observed in *I. Waxman & Sons.*[8], there is support in the case law for the proposition that equity may become debt. For instance, in that case, I held that a judgment obtained at the suit of a shareholder constituted debt. An analysis of the nature of the claims is therefore required. If the claims fall within the parameters of section 2 of the *CCAA*, clearly they are to be treated as equity claims and not as debt claims.

[33] In this case, in essence the claims of the preferred shareholders are for one or a combination of the following:

(a) declared but unpaid dividends;

(b) unperformed requests for redemption;

(c) compensatory damages for the loss resulting in the purchased preferred shares now being worthless and claimed to have been caused by the negligent or fraudulent

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[8] (2008), 2008 CarswellOnt 1245.

misrepresentation of Nelson or of persons for whom Nelson is legally responsible; and

(d) payment of the amounts due upon the rescission or annulment of the purchase or subscription for preferred shares.

[34] In my view, all of these claims fall within the ambit of section 2, are governed by sections 6(8) and 22.1 of the *CCAA,* and therefore do not constitute a claim provable for the purposes of the statute. The language of section 2 is clear and unambiguous and equity claims include "a claim that is in respect of an equity interest" and a claim for a dividend or similar payment and a claim for rescission. This encompasses the claims of all of the preferred shareholders including the Styles whose claim largely amounts to a request for rescission or is in respect of an equity interest. The case of *National Bank of Canada v. Merit Energy Ltd.*[9] is applicable in regard to the latter. In substance, the Styles' claim is for an equity obligation. At a minimum, it is a claim in respect of an equity interest as described in section 2 of the CCAA. Parliament's intention is clear and the types of claims advanced in this case by the preferred shareholders are captured by the language of the amended statute. While some, and most notably Professor Janis Sarra[10], advocated a statutory amendment that provided for some judicial flexibility in cases involving damages arising from egregious conduct on the part of a debtor corporation and its officers, Parliament opted not to include such a provision. Sections 6(8) and

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[9] Supra, note 5.

[10] "From Subordination to Parity: An International Comparison of Equity Securities Law Claims in Insolvency Proceedings" (2007) 16 Int. Insolv. Re., 181.

22.1 allow for little if any flexibility. That said, they do provide for greater certainty in the appropriate treatment to be accorded equity claims.

[35] There are two possible exceptions. Mr. McVey claims that his promissory note should never have been converted into preference shares, the conversion was unauthorized and that the signatures on the term sheets are not his own. If Mr. McVey's evidence is accepted, his claim would be qua creditor and not preferred shareholder. Secondly, it is possible that monthly dividends that may have been lent to Nelson by Larry Debono constitute debt claims. The factual record on these two possible exceptions is incomplete. The Monitor is to investigate both scenarios, consider a resolution of same, and report back to the court on notice to any affected parties.

[36] Additionally, the claims procedure will have to be amended. The Monitor should consider an appropriate approach and make a recommendation to the court to accommodate the needs of the stakeholders. The relief requested in the notice of motion is therefore granted subject to the two aforesaid possible exceptions.

Pepall J.

Released: November 16, 2010

CITATION: Nelson Financial Group Ltd., 2010 ONSC 6229
COURT FILE NO.: 10-8630-00CL
DATE: 20101116

ONTARIO

SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

BETWEEN:

IN THE MATTER OF THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, C-36, AS AMENDED

AND IN THE MATTER OFA PLAN OF COMPROMISE OR ARRANGEMENT OF NELSON FINANCIAL GROUP LTD.

REASONS FOR JUDGMENT

Pepall J.

Released: November 16, 2010

TAB 3

COURT FILE NO.: 04-CL-5306
DATE: 20060120

SUPERIOR COURT OF JUSTICE - ONTARIO
(Commercial List)

RE: IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PROPOSED PLAN OF COMPROMISE OR ARRANGEMENT WITH RESPECT TO STELCO INC. AND THE OTHER APPLICANTS LISTED IN SCHEDULE "A"

APPLICATION UNDER THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

BEFORE: FARLEY J.

COUNSEL: Michael Barrack, James D. Gage and Geoff R. Hall, for the Applicants
Robert Thornton and Kyla Mahar, for the Monitor
Peter Jervis, George Glezos and Karen Kiang, for the Equity Holders
John Varley, for the Salaried Employees
David Jacobs, for USW Locals 8782 and 5328
Aubrey Kauffman, for Tricap Management Ltd.
Kevin Zych and Rick Orzy, for the 8% and 10.4% Stelco Bondholders
Lawrence Thacker, for the Directors of Stelco
Sharon White, for USW Local 1005
Ken Rosenberg, for USW International
Kevin McElcheran, for GE
Gale Rubenstein and Fred Myers, for the Superintendent of Financial Services
Derrick Tay, for Mittal
David R. Byers and Sean Dunphy, for CIT Business Credit as DIP and ABL Lender
V. Gauthier, for BABC Global Finance
L. Edwards, for EDS Canada Inc.
Peter Jacobsen, for Globe & Mail
Paul Macdonald and Andy Kent, for Sunrise and Appalloosa
Murray Gold and Andrew Hatnay, for the Salaried Retirees
Flaviano Stanc, Self-Represented

HEARD: January 17-18, 2006, with further information January 20, 2006

ENDORSEMENT

(Motion by the Applicants for a Sanction Order and Cross-Motion of Certain Equity Holders)

[1] The Applicants (collectively "Stelco") moved for:

(a) a declaration that Stelco has complied with the provisions of the *Companies' Creditors Arrangement Act* ("CCAA") and the orders of this court made in this CCAA proceeding;

(b) a declaration that the Stelco plan of arrangement pursuant to the CCAA and the reorganization of Stelco Inc. ("S") under the *Canada Business Corporations Act* ("CBCA") (collectively the "Plan") as voted on by the affected creditors of Stelco is fair and reasonable;

(c) an order sanctioning and approving the Plan; and

(d) an order extending the Stay Period and Stay Date in the Initial Order until March 31, 2006.

[2] This relief was unopposed by any of the stakeholders except for various existing shareholders of S (who may also be employees or retirees of Stelco). In particular there was organized objection to the Plan, especially as in essence the Plan would eliminate the existing shareholders, by a group of shareholders (AGF Management Ltd., Stephen Stow, Pollitt & Co., Levi Giesbrecht, Joe Falco and Phil Dawson) who have styled themselves as "The Equity Holders" ("EH"). On December 23, 2005 the EH brought in essence a cross motion seeking the following relief:

(a) An order extending the powers of the Monitor, Ernst & Young, in order to conduct a sale of the entire Stelco enterprise as a going concern through a sale of the common shares or assets of Stelco on such terms and conditions as are considered fair;

(b) An order authorizing and directing the Monitor to implement and to take all steps necessary to complete and fulfill all requirements, terms, conditions and steps of such a sale;

(c) An order authorizing and directing the Monitor to conduct the sale process in accordance with a plan for the sale process approved by the court;

(d) An order directing the Monitor to retain such fully independent financial advisors and other advisors as necessary to conduct this sale process;

(e) An order confirming that the powers granted herein to the Monitor supersede any provision of any prior Order of this Court made in the within proceedings to the extent that such provision of any prior order is inconsistent with or contradictory to this order, or would otherwise limit or hinder the power and authority granted to the Monitor;

(f) An order directing Stelco and its directors, officers, counsel, agents, professional advisors and employees, and its Chief Restructuring Officer, to cooperate fully with the Monitor with regard to this sale process, and to provide the Monitor with such assistance as may be requested by the Monitor or its independent advisors;

(g) In the alternative, an order suspending the sanctioning of the Proposed Plan of Arrangement, approved by the creditors on December 9, 2005, for a period of two months from the date of such order, so that the Monitor may conduct the independent sale process that may result in a more profitable outcome for all stakeholders, including the Equity Holders;

(h) In the further alternative, an order lifting the *Companies' Creditors Arrangement Act* stay of proceedings in respect of Stelco without approving the Plan of Arrangement, as approved by the creditors on December 9, 2005, pursuant to such terms as are just and are directed by court; and

(i) Such further and other relief as counsel may advise and this Honourable Court may permit.

[3] In its factum, the EH requested that the court adjourn approval of the Plan for 60 days and direct the Monitor to conduct an independent sale process for the shares of S. In the attendances on January 17 and 18, 2006, the EH then asked that approval of the Plan be adjourned for 30 days in order to see if there were expressions of interest for the shares of S forthcoming in the interim.

[4] I indicated that I would defer my consideration of the adjournment request until after I had had submissions on the motions before me as set out above. I also indicated that while there did not appear to be any concern by anyone including the EH as to the first two elements concerning CCAA plan sanctioning as discussed in *Re Algoma Steel Inc.* (2001), 30 C.B.R. (4^{th}) 1 (Ont. S.C.J.) at p. 3:

> In a sanction hearing under the *Companies' Creditors Arrangement Act* ("CCAA") the general principles to be applied in the exercise of the court's discretion are:
>
> (a) There must be strict compliance with all statutory requirements and adherence to the previous orders of the court;

> (b) All materials filed and procedures carried out must be examined to determine if anything has been done or purported to be done which is not authorized by the CCAA; and
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> (c) The Plan must be fair and reasonable.
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> See *Northland Properties Ltd., Re* (1988), 73 C.B.R. (N.S.) 175 (B.C. S.C.), affirmed *Northland Properties Ltd. v. Excelsior Life Insurance Co. of Canada* (1989), 73 C.B.R. (N.S.) 195 (B.C. C.A.) at p. 201; *Campeau Corp., Re* (1992), 10 C.B.R. (3d) 104 (Ont. Gen. Div.) at p. 109; *Olympia & York Developments Ltd. v. Royal Trust Co.* (1993), 12 O.R. (3d) 500 (Ont. Gen. Div.) at p. 506; *Sammi Atlas Inc., Re* (1998), 3 C.B.R. (4th) 171 (Ont. Gen. Div. [Commercial List]), at pp. 172-3; *Canadian Airlines Corp., Re*, [2000] 10 W.W.R. 269 (Alta. Q.B.), leave to appeal dismissed, [2000] 10 W.W.R. 314 (Alta. C.A. [In Chambers]).

it would not be sufficient to only deal in this hearing with the third test of whether the Plan was fair and reasonable (including the aspect of "fair, reasonable and equitable" as discussed in *Sammi*). Rather the court also had to be concerned as to whether the Plan was implementable. In other words, it would be futile and useless for the court to approve a plan which stood no reasonable prospect of being implemented. That concern of the court had been raised by my having been alerted by the Monitor in its 46th Report at paragraphs 8-9:

> 8. The Monitor has had discussions with the proposed ABL lenders, Tricap, the Province and Stelco regarding the status of the ABL Loan and the Bridge Loan. The Monitor has been advised that the parties are continuing to work at resolving issues that are outstanding as at the date of this Forty-Sixth Report. However, all of the parties remain optimistic that acceptable solutions to the outstanding issues will be found and implemented.
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> 9. In the Monitor's view, the principal issues to be resolved include:
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> (a) the corporate structure of Stelco, which could involve the transfer of assets of some of the operations or divisions of the Applicants to new affiliates; and
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> (b) satisfying the ABL lenders and Tricap as to the priority of the new financing.
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> These issues need to be resolved primarily among the proposed ABL lenders, Tricap and Stelco and will also involve the Province insofar as they affect pension and related liabilities.

[5] I was particularly disquieted by the lack of progress in dealing with these outstanding matters despite the passage of 39 days since the Plan was positively voted on December 9, 2005. I do appreciate that Christmas, Hanukkah and New Year's were celebrated in this interval and that there had been a certain "negotiation fatigue" leading up to the December 9th revisions to the Plan and that I have advocated that counsel, other professionals and litigation participants balance their lives and pay particular attention to family and health. However I find it unfortunate that there would appear to have been such a lengthy hiatus, especially when the workers at Stelco continued (as they have for the past two years while Stelco has been under CCAA protection) to produce steel in record amounts. I therefore demanded that evidence be produced forthwith to demonstrate to my satisfaction that progress was real and substantial so that I could be satisfied about implementability. As a side note I would observe that in the "normal" case, sanction orders are typically sought within two or three days of a positive creditor vote so that it is not unusual for documentation to be sorted out for a month before a plan is implemented with a closing.

[6] The EH filed material to support its submission that the Plan is not fair, reasonable and equitable because it is alleged that there is currently sufficient value in Stelco to fully satisfy the claims of affected and unaffected creditors and to provide at least some value to current shareholders. The EH prefers to have a search for some entity to take out the current shareholders for "value". Fabrice Taylor, a chartered financial analyst with Pollit & Co. swore an affidavit on the eve of this hearing which was sent electronically to the service list on January 16, 2006 at approximately 7:30 p.m. In that affidavit, he states:

> 2. The Dofasco bidding war has highlighted a crucial fact about steel asset valuations, notably that strategic buyers place a much higher value on them than public market investors. Attached as Exhibit "1" is an article entitled "Restructuring of steel industry revives investors' interest", published in the Financial Times on December 14, 2005.
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> 3. I, along with Murray Pollitt and a number of Stelco shareholders, have spent the past three months attempting to attract strategic buyers and/or equity investors in Stelco. These strategic buyers and equity investors are mostly international. Some had already considered buying Stelco or had made bids for the company but had stopped following the story some months ago. Others were not very familiar with Stelco.
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> 4. Three factors hindered our efforts. First, Stelco is under CCAA protection, a complicated situation involving multiple players and interests (unions, politics, pensions) that is difficult to understand, particularly for foreigners. Second, there has not been enough time for these strategic buyers or equity investors to deepen their understanding or to perform due diligence. Finally, the Dofasco bid process, while providing emphatic evidence that steel assets are increasingly valuable, hinders certain strategic buyers and financial

institutions interested in participating in Stelco because they are distracted and/or conflicted by the Dofasco sale. I have been advised by some of the participants in the Dofasco negotiations that they would be willing to carefully consider a Stelco transaction once the Dofasco sale has been resolved.

5. The Forty Fifth Report of the Monitor confirmed that Stelco had not received any offers in the last several months. The report does not answer the question of whether the company or its financial advisors have in fact attempted to attract any offers. I believe that Stelco would have received expressions of interest had the company made efforts to attract offers, or had the Dofasco sale been resolved earlier. I believe that the Monitor should be authorized, for a period of at least 60 days, to canvas interest in a sale of Stelco before the approval of the proposed plan of restructuring.

[7] No satisfactory explanation was forthcoming as to why this affidavit, if it needed to be filed at all, was not served and filed by December 23, 2005, in accordance with the timetable which the EH and the other stakeholders agreed to. Certainly there is nothing in the affidavit which is such late breaking news that this deadline could not have been met, let alone that it was served mere hours before the hearing commenced on January 17, 2006. Aside from the fact that the financing arrangements forming the basis of the Plan contained "no shop" covenants which would make it inappropriate and a breach to try to attract other offers, the foregoing excerpts from the Taylor affidavit clearly illustrate that despite apparently diligent efforts by the EH, no one has shown any real or realistic interest in Stelco. Reading between the lines and without undue speculation, it would appear that the efforts of the EH were merely politely rebuffed.

[8] Certainly Stelco is not Dofasco, nor is it truly a comparable (as opposed to a contrastor). Stelco has been a wobbly company for a long time. Further as I indicated in my October 3, 2005 endorsement, in the preceding 20 months under the CCAA protection, Stelco has become "shopped worn". The unusual elevation of steel prices in the past two years has helped Stelco avoid the looming liquidity crisis which it anticipated in its CCAA filing on January 29, 2004. However even this financial transfusion has not allowed it to become a healthy company or truly given it a burgeoning war chest to weather bad times the way that other steel companies (including some in Canada) have so benefited. The redness of the visage of Stelco is not a true indication of health and well being; rather it seems that it is rouge to mask a deep pallor.

[9] I am satisfied on the evidence of Hap Stephen, the Chief Restructuring Officer of Stelco and of the Monitor that there has been compliance with all statutory requirements and adherence to previous orders of the court and further that nothing has been done or purported to be done that is not authorized by the CCAA.

[10] The next question to be dealt with is whether the Plan is fair, reasonable and equitable. I was advised that creditors of the affected creditor classes representing approximately 90% in value of each class voted on the Plan. The Monitor reported at para. 19 of its 44th Report as to the results of the vote held December 9th as follows:

Class of Affected Creditors	**Percentage in favour by Number**	**Percentage in favour by Dollar Value**
Stelco	78.4%	87.7%
Stelwire	89.01%	83.47%
Stelpipe	94.38%	86.71%
CHT Steel	100%	100%
Welland Pipe	100%	100%

[11] This favourable vote by the affected creditors is substantially in excess of the statutory two-thirds requirement. By itself that type of vote, particularly with such a large quorum present, would ordinarily be very convincing for a court not interfering with the informed decisions of business people. With that guideline, plus the aspect that a plan need not be perfect, together with the lack of any affected creditor opposition to the Plan being sanctioned and the fact that the Plan including its ingredients and nature and amount of compromise compensation to be given to affected creditors having been exhaustively negotiated in hard bargaining by the larger creditor groups who are recognized as generally being sophisticated and experienced in this area, and the consideration of the elements in the next paragraph, it would seem to me that the Plan is fair, reasonable and equitable vis-à-vis the affected creditors and I so find. See *Sammi*, at p. 173; *Re T. Eaton Co.* (1999), 15 C.B.R. (4th) 311 (Ont. S.C.J.) at p. 313; *Re Olympia & York Developments Ltd.* (1993), 12 O.R. (3d) 500 (Gen. Div) at p. 510.

[12] I also think it helpful to examine the situation pursuant to the analysis which Paperny J. did in *Re Canadian Airlines Corp.* (2000), 20 C.B.R. (4th) 1 (Alta. Q.B.), leave to appeal refused (2000), 20 C.B.R. (4th) 46 (Alta C.A. [In Chambers]). That proceeding also involved an application pursuant to the corporate legislation, the *Business Corporations Act* (*Alberta*), concerning the shares and shareholders of Canadian Airlines. In that case, Paperny J. found the following factors to be relevant:

(a) the composition of the vote: claims must have been properly classified, with no secret arrangements to give an advantage to a creditor or creditors; approval of the plan by the requisite majority of creditors is most important (in the case before me of Stelco: the challenge to classification was dismissed; there was no suggestion of secret arrangements; and, as discussed above, the quorum and size of the positive vote were very high);

(b) anticipated receipts in liquidation or bankruptcy: it is helpful if the Monitor or other disinterested person has prepared a liquidation analysis (in Stelco, the Monitor determined that on liquidation, affected creditor recovery would likely range from 13 to 28 cents on the dollar; it should also be observed that Stelco has engaged in extensive testing of the market as to possible capital raising or sale with the aid of established firms and professionals of great experience and had come up dry.);

(c) alternatives to the proposed plan: it is significant if other options have been explored and rejected as unworkable (in Stelco; see comment in (b));

(d) oppression of the rights of certain creditors (in Stelco, this was not a live issue as nothing of this sort was alleged);

(e) unfairness to shareholders (in Stelco, this will be dealt with later in my reasons; however allow me to observe that the interests of shareholders becomes engaged if they are not so far underwater that there is a reasonable prospect in the foreseeable future that the fortunes of a company would otherwise likely be turned around so that they would not continue to be submerged); and

(f) the public interest: the retention of jobs for employees and the support of the plan by the company's unions is important (in Stelco, the Plan does not call for reductions in employment; there is provision for continuation of the capital expenditure program and its funding; an important enterprise for the municipal and provincial levels of government would be preserved with continuing benefits for those communities; an important customer and supplier would continue in the industry and maintain competition; the USW International Union and its locals (except for local 1005) supported the Plan and indeed were instrumental in bringing Tricap Management Limited to the table (local 1005's position was that it did not wish to engage in the CCAA process in any meaningful way as it was content to rely upon its existing collective agreement which now still has several months to go before expiring).

However that is not the end of that issue: what of the shareholders?

[13] Is the Plan fair, reasonable and equitable for the existing shareholders of S? They will be wiped out under the Plan and their shares eliminated. New equity will be created in which the existing shareholders will not participate. They have not been allowed to vote on the Plan.

[14] It is well established that a reorganization pursuant to s. 191 of the CBCA may be made in conjunction with a sanction order under the CCAA and that such a reorganization may result in the cancellation of existing shares of the reorganized corporation based on those shares/equity having no present value (in the sense of both value "now" and the likelihood of same having value in the reasonably foreseeable future, absent the reorganization including new debt and equity injections and permitted indulgences or other considerations and adjustments). See *Re Beatrice Foods Inc.* (1996), 43 C.B.R. (4th) 10 (Ont. Gen. Div.) at para. 10-15; *Re Laidlaw Inc.* (2003), 39 C.B.R. (4th) 230 (Ont. S.J.C.); *Algoma* at para. 7; *Cable Satisfaction International Inc. v. Richter & Associés Inc.* (2004), 48 C.B.R. (4th) 205 (Que. S.C.) at p. 217. The Dickenson Report, which articulated the basis for the reform of corporate law that resulted in the enactment of the CBCA, described the object of s. 191 as being:

> to enable the court to effect any necessary amendment to the articles of the corporation in order to achieve the objective of the reorganization without having to comply with all the formalities of the Draft Act, <u>particularly shareholder approval of the proposed amendment</u> (emphasis added): R.W.V. Dickenson, J.L. Howard, L. Getz, *Proposals for a New Business Corporations Law for Canada*, vol. 1 (Ottawa: Information Canada. 1971) at p. 124.

[15] The fairness, reasonableness and equitable aspects of a plan must be assessed in the context of the hierarchy of interests recognized by insolvency legislation and jurisprudence. See *Canadian Airlines* at pp. 36-7 where Paperny J. stated:

> Where a company is insolvent, only the creditors maintain a meaningful stake in its assets. Through the mechanism of liquidation or insolvency legislation, the interests of shareholders are pushed to the bottom rung of the priority ladder. The expectations of creditors and shareholders must be viewed and measured against an altered financial and legal landscape. Shareholders cannot reasonably expect to maintain a financial interest in an insolvent company where creditors' claims are not being paid in full. It is through the lens of insolvency that the court must consider whether the acts of the company are in fact oppressive, unfairly prejudicial or unfairly disregarded. CCAA proceedings have recognized that shareholders may not have "a true interest to be protected" because there is no reasonable prospect of economic value to be realized by the shareholders given the existing financial misfortunes of the company: *Royal Oak Mines Ltd.*, *supra*, para. 4., *Re Cadillac Fairview Inc.* (March 7, 1995), Doc. B28/95 (Ont. Gen. Div. [Commercial List]), and *T. Eaton Company*, *supra*.
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> To avail itself of the protection of the CCAA, a company must be insolvent. The CCAA considers the hierarchy of interests and assesses fairness and reasonableness in that context. The court's mandate not to sanction a plan in the absence of fairness necessitates the determination as to whether the complaints of dissenting creditors and shareholders are legitimate, bearing in mind the company's financial state. The articulated

> purpose of the Act and the jurisprudence interpreting it, "widens the lens" to balance a broader range of interests that includes creditors and shareholders and beyond to the company, the employees and the public, and tests the fairness of the plan with reference to its impact on all of the constituents.
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> It is through the lens of insolvency legislation that the rights and interests of both shareholders and creditors must be considered. The reduction or elimination of rights of both groups is a function of the insolvency and not of oppressive conduct in the operation of the CCAA. The antithesis of oppression is fairness, the guiding test for judicial sanction. If a plan unfairly disregards or is unfairly prejudicial it will not be approved. However, the court retains the power to compromise or prejudice rights to effect a broader purpose, the restructuring of an insolvent company, provided that the plan does so in a fair manner."

[16] The question then is does the equity presently existing in S have true value at the present time independent of the Plan and what the Plan brings to the table? If it does then the interests of the EH and the other existing shareholders must be considered appropriately in the Plan. This is fairly put in K.P. McElcheran, *Commercial Insolvency in Canada* (Toronto, Lexis Nexis Canada Inc.: 2005) at p. 290 as:

> If, at the time of the sanction hearing, the business and assets of the debtor have a value greater than the claims of the creditors, a plan of arrangement would not be fair and reasonable if it did not offer fair consideration to the shareholders.

[17] However if the shareholders truly have no economic interest to protect (keeping in mind that insolvency and the depth of that insolvency may vary according to which particular test of insolvency is applied in respect of a CCAA proceeding: as to which, see *Re Stelco Inc.*, [2004] O.J. No. 1257 (S.C.J. [Commercial List]), leave to appeal dismissed [2004] O.J. No. 1903 (C.A.), leave to appeal dismissed (S.C.C.) No. 30447). In *Cable Satisfaction*, Chaput J. at p. 218 observed that when shareholders have no economic interest to protect, then they have no claim to a right under the proposed arrangement and the "[m]ore so when, as in the present case, the shareholders are not contributing to any of the funding required by the Plan." I do note in the case of the Stelco Plan and the events leading up to it, including the capital raising and sale processes, that despite talk of an equity financing by certain shareholders, including the EH, no concrete offer ever surfaced.

[18] If the existing equity has no true value at present, then what is to be gained by putting off to tomorrow (the ever present and continuous problem in these proceedings of manãna - which never comes) what should be done today. The EH speculate, with no concrete basis for foundation as demonstrably illustrated by the eve of hearing Taylor affidavit discussed above, that something good may happen. I am of the view that that approach was accurately described in court by one counsel as a desperation Hail Mary pass and the willingness of someone, without any of his own chips, in the poker game willing to bet the farm of someone else who does have an economic interest in Stelco.

[19] I also think it fair to observe that in the determination of whether someone has an economic value, that analysis should be conducted on a reasonable and probable basis. In a somewhat different but applicable context, I observed in *New Quebec Raglan Mines Ltd. v. Blok-Andersen*, [1993] O.J. No. 727 at p. 3:

> The "highest price" is not the price which could be derived on the basis of the most optimistic and risky assumptions without any regard as to their likelihood of being realized. It also seems to me that prudence would involve a consideration that there be certain fall back positions. Even in betting on horses, the most savvy and luckiest punter will not continue to stake all his winnings of the previous race on the next (and so on). If he does, he will go home wearing the barrel before the last race is run.

Alternatively there is a saying: "If wishes were horses, then beggars would ride."

[20] Unless I were to now dismiss the motion for sanctioning and approving the Plan because I found that it was not implementable and/or that it was not fair, reasonable and equitable to the existing shareholders (based upon the proviso that I did determine that the existing shareholders did have a valid present material equity of value), then I see no reason not to dismiss the motion of the EH concerning its request for an adjournment and its request for a further sale (or other related disposition) process. Allow me to observe that no matter how well intentioned the motion of the EH in that regard, I find that that request to be lacking in any valid substance. Rather, the evidence presented was in essence a chimera. I think it fair to observe that, with all the capital raising and sales processes to date which Stelco has undertaken in conjunction with its experienced and well placed professional advisers together with its Chief Restructuring Officer and the Monitor, the bushes have been exhaustively and well beaten as to any real possible interest. Despite three months of what one must presume to be diligent efforts, the EH have come up with nothing concrete. I do not find that the three factors mentioned by Taylor in his late-blooming affidavit of January 16th to be remotely close to convincing. The first two, if taken at face value, would lead one to the conclusion that no one has the time, interest or ability to take an interest in Stelco in any meaningful timeframe. The third presumes that the losing bidder for Dofasco, be it Arcelor or ThyssenKrupp, will almost automatically want Stelco - and at a price and upon terms which would result in present equity being attributed value. I must say in fairness that this is wishful thinking as neither of these warring bidders pursued any interest in Stelco during the previous processes. It is neither clear nor obvious why mere municipal proximity of Dofasco to Stelco's Hilton Works in Hamilton would now ignite any interest in Stelco.

[21] I also think it fair to observe that not proceeding with the sanction hearing now and indeed starting a brand new search for someone who will think Stelco so worthwhile that it will offer such a large amount (with or without onerous conditions) is akin to someone coming into court when a receiver is seeking court approval on a sale - and that someone being allowed to know the price and conditions - and then being able to make an offer for a price somewhat higher. (I reiterate that here we do not even have an offer or a price.) I do not see that such a procedure would be consistent with the principles laid out in *Royal Bank*

v. Soundair Corp. (1991), 7 C.B.R. (3d) 1 (Ont. C.A.). Given that the affected creditors have rather resoundingly voted in favour of the Plan, all in accordance with the provisions of the CCAA and the Court orders affecting the sanction, I would be of the view that if the existing equity has no value, then the EH's request in this respect would, if granted, be of significant detriment to the integrity of the insolvency system and regime. I would find that inappropriate to attempt to justify proceeding along that line.

[22] Allow me to return to the pivotal point concerning the question of whether the Plan is fair, reasonable and equitable, vis-à-vis the existing equity. The EH retained Navigant Consulting which relied upon the views of Metal Bulletin Research ("MBR") which, *inter alia*, predicted a selling spot price of hot roll steel at $525 U.S. per ton. Navigant's conclusion in its December 8, 2005 report was that the value of residual shareholder equity was between $1.1 to $1.3 billion or a per share value of between $10.76 and $12.71. However, when Stelco pointed out certain deficiencies in this analysis, Navigant took some of these into account and reduced its assessment of value to between $745 million to $945 million for residual shareholder value on per share value of $7.29 to $9.24, using a discounted cash flow ("DCF") approach. Navigant tested the DCF approach against the EBITDA approach. It is interesting to note that on the EBITDA analysis approach Navigant only comes up to a conclusion that the equity is valued at $8 million to $83 million or $0.09 to $0.81 per share. If the Court were to accept that as an accurate valuation, or something at least of positive value even if not in that neighbourhood, then I would have to take into account existing shareholder interests in determining whether the Plan was fair, reasonable and equitable – and not only vis-à-vis the affected creditors but also vis-à-vis the interests of the existing shareholders given that at least some of their equity would be above water. I understand the pain and disappointment of the existing shareholders, particularly those who have worked hard and long with perhaps their life savings tied up in S shares, but regretfully for them I am not able to come to a conclusion that the existing equity has a true positive value.

[23] The fight in the Stelco CCAA proceedings has been long and hard. No holds have been barred as major affected creditors have scrapped to maximize their recovery. There were direct protracted negotiations between a number of major affected creditors and the new equity sponsors under the Plan, all of whom had access to the confidential information of Stelco pursuant to Non Disclosure Agreements. These negotiations established a value of $5.50 per share for the <u>new</u> common shares of a <u>restructured</u> Stelco. That translates into an enterprise value (not an equity value since debt/liabilities must be taken into consideration) of $816.6 million for Stelco, or a recovery of approximately 65% for affected creditors. The parties engaged in these negotiations are sophisticated experienced enterprises. There would be no particular reason to believe that in the competition involved here that realistic values were ignored. Further, the affected creditors generally were rather resoundingly of the view by their vote that an anticipated 65% recovery was as good as they could reasonably expect.

[24] The 45th Report of the Monitor had a chart of calculations to determine the level of recovery of affected creditors at various assumed enterprise values up to and including the top end of Navigant's range of enterprise value (as contrasted with residual equity value).

At the high end of Navigant's range of revised enterprise value, $1.6 billion, the Monitor calculated that affected creditors would still not receive full recovery of their claims.

[25] The EH cited the sale of the EDS Canada claim to Tricap as being at a premium as evidence in support of Navigant's conclusion. However, the fact was that this claim was purchased not at a premium, but rather at a discount. That would be confirmation of the opposite of which the EH has been contending.

[26] Despite a very comprehensive capital raising and asset sale process, with the market alerted and well canvassed, and with the ability to conduct due diligence, no interested party came forwarded to conclude a deal. Even since the December 9, 2005 vote when the terms of the Plan were available, no interested party has come forward with any expression of interest which would attribute value to the existing shareholders.

[27] Stelco's experts, UBS and BMO Nesbit Burns, both have given opinions that there is no value to the existing equity. Their expert opinions were not challenged by cross-examination. Both these advisors are large sophisticated institutions; both have extensive experience in the steel industry.

[28] UBS calculated the enterprise value of Stelco as being in the range of $550 million to $750 million; BMO Nesbitt Burns at $650 million to $850 million. On that basis the unsecured creditors would receive less than full recovery of their claims, which would lead to the conclusion that there is no value for the existing shareholders. The Monitor commissioned an independent estimate of the enterprise value from its affiliate, Ernst & Young Orenda Corporate Finance Inc's Valuation Group. That opinion came in at $635 million to $785 million.

[29] I would note that Farley Cohen, the principal author of the Navigant report, does not have experience in dealing with integrated steel companies. I find it unusual that he would have customized his approach in calculating equity value by not deducting the Asset Based Lenders loan. Brad Fraser of BMO Nesbitt Burns stated that such customization was contrary to the practice at his firms both present and past and that the Navigant's approach was internally inconsistent with respect thereto as to 2005 to 2009 cash flows as contrasted with terminal value. The Navigant report appears to have forecasted a high selling price for steel combined with low costs for imports such as coal and scrap, which would be contrary to historical complementary movements between steel prices and these inputs.

[30] Navigant relies on an average price of $525 US per ton as provided by MBR. This is a single source as to this forecast. While a single analyst may come up with a forecast which is shown by the passage of time to be dead on accurate, it would seem to me to be more realistic and prudent to rely on the consensus approach of considering the views of a greater number of "representative" analysts, especially when prices appear volatile for the foreseeable future. That consensus approach allows for consideration of the way that each analyst looks at the market and the factors and weights to be given. The UBS opinion reviewed the pricing forecast of eight analysts and BMO Nesbitt Burns' ten analysts.

Interestingly, MBR's choice of a price at the top of the band would seem at odds as the statements on the MBR website foreseeing downward pressure on steel prices in 2006 because of falling prices in China; although this inconsistency was pointed out, there was no response forthcoming.

[31] Navigant estimated Stelco's financial performance for the last quarter of 2005 and made a significant upward adjustment. However, the actual experience would appear to indicate that such an adjustment would overstate Stelco's results by $124 million.

[32] Navigant's DCF approach involved a calculation of Stelco's enterprise value by adding the present value of a stream of cash flow from the present to 2009 and the present value of the terminal value determined as at 2009 so that the terminal value represents the majority (60% approximately) of enterprise value as calculated by Navigant. MBR chose a 53-year average steel price despite significant changes over that time in the industry. However, coal and scrap costs were determined as at 2009. This produced the anomalous result that steel prices are rising while costs are falling. This would imply great structural difficulties (economically and functionally) in the steel industry generally and a lack of competition. A terminal value EBITDA margin for Stelco would then be implied at approximately 26% or some 11% higher than the EBITDA margin actually achieved by Stelco in the first quarter of 2005, the most profitable quarter in the history of Stelco.

[33] Interestingly, since Navigant's approach in fact would decrease calculated value, UBS and BMO Nesbitt Burns used a weighted average cost of capital ("WACC") for Stelco in the range of 10% to 14%; Navigant used 24%. A higher WACC will result, all other things being equal, in a lower enterprise value. Navigant considered that there should be a 10% to 15% company-specific premium because of the risks associated with Stelco vis-à-vis the higher steel prices forecast by MBR. This would appear to imply that there was recognition that either MBR was aggressive in its forecasting or that price volatility would caution one to use consensus forecasting. Colin Osborne, a senior executive of Stelco, with considerable experience in the steel industry provided direct evidence on the substantial differences between each of Stelco, AK Steel, U.S. Steel and Algoma. Mr. Cohen acknowledged in cross-examination that these differences made Dofasco a more valuable company than Stelco. As set out at para. 74 of the Stelco Factum:

> 74. The specific difference identified by Mr. Osborne which made Dofasco unique include but are not limited to:
>
> (a) non-union, flexible work environment (vs. Stelco, Algoma, AK Steel and U.S. Steel);
>
> (b) legacy costs which are very low due to non-conventional profit sharing, which limits liability (vs. Stelco, AK Steel, Algoma and U.S. Steel);
>
> (c) high historical cap-ex spend per ton (vs. Stelco, Algoma and U.S. Steel);

(d) a flexible steelmaking stream in terms of a hybrid EAF and blast furnace BOF stream in Hamilton and a mini-mill operation in the U.S. (vs. Stelco, Algoma, U.S. Steel and AK Steel which are all blast furnace based steel makers);

(e) a value added product mix focused on coated products and tubing (vs. Stelco and Algoma which focus on hot roll); and

(f) a strong raw material position with excess iron ore and self-sufficiency in coke (Algoma, Stelco and AK Steel all have dependence to various degrees on either iron ore or coke or both).

Dofasco and Stelco are not in my view fungible. There are incredible differences between these two enterprises, to the disadvantage of Stelco.

[34] The reply affidavit of Mr. Fraser of BMO Nesbitt Burns calculated the effect of all of the acknowledged corrections to the initial Navigant report and other adjustments. The result of this exercise was a conclusion by him that there was no value available for existing shareholders. This, along with all the other affidavits provided on the Stelco side, was not cross-examined on.

[35] While not referred to in the Factum of EH, there were a number of quite serious allegations raised in material filed by the EH against management of Stelco concerning bias and manipulation. Mr. Osborne responded to each of these allegations; he was not cross-examined. I find it unfortunate that such allegations appear to have been made on an unsubstantiated shotgun approach.

[36] The position of the EH is that certain of the features of the Plan should be assumed as transportable directly and without change into a scenario where some insolvency rescuer emerges on the scene as the equivalent of a White Knight, one it would seem which has been awakened from slumber. I am of the view that presumes too much. For example, I take it that the Province would not automatically accept this potential newcomer without question; nor would it likely relish the resumption of weeks of hard bargaining. I would think it unwise, impudent and high stakes poker (with other peoples' money) to speculate as did Taylor in para. 41 of his December 23, 2005 affidavit:

> 41. Were Stelco to emerge from CCAA protection and were the province to carry out its threat to revoke Stelco's entitlement to the benefit of section 5.1 the end result would likely be a liquidation of the company. The Province would be responsible for a substantial portion of Stelco's pension promise. It would clearly not be in the Province's self-interest to force Stelco into liquidation. It was, in other words, an obvious bluff. Yet the notion of calling this bluff does not appear to have crossed management's mind.

This should be contrasted with the views of the Monitor in its 44th Report at para. 61:

> 61. It should also be noted that the Pension Plan Funding Arrangements and the $150 million New Province Note embodied in the Approved Plan were agreed to by the Province only in the context of the terms of the Approved Plan and, in particular, the capital structure, liquidity and other elements contemplated therein. The Province has advised that its proposed financing and the Pension Plan Funding Arrangements should not be assumed to be available if any of the elements of the Approved Plan are changed.

[37] The end result is that given the above analysis, I have no hesitation in concluding that it would be preferable to rely upon the analysis of UBS, BMO Nesbitt Burns and Ernst & Young Orenda, both as to their direct views as to the enterprise value of existing Stelco and as to their criticism of the Navigant and MBR reports concerning Stelco. Therefore, I conclude that the existing shareholders cannot lay claim to there being any existing equity value. Given that conclusion, it would be inappropriate to justify cutting in these existing shareholders for any piece of the emergent restructured Stelco. If that were to happen, especially given the relative values and the depth of submersion of existing equity, then it would be unfair, unreasonable and inequitable for the affected creditors.

[38] That then leaves the remaining question: Does it appear likely that the Plan will be implementable? I have been advised on Wednesday, January 18th that I would receive executed term sheets (which would address the issues raised by the Monitor discussed above) by 5 p.m., Friday, January 20th.

[39] The motion and adjournment request of the EH is dismissed.

[40] There was a request to extend the stay to March 31, 2006. I am of the view that it would be sufficient and desirable to extend the stay (subject, of course, to further extension) to March 3, 2006.

[41] I have received the term sheets together with the Monitor's 48th Report by the 5 p.m. January 20th deadline and find them satisfactory as demonstrating to my analysis and satisfaction that the Plan is implementable as discussed above, subject to a comeback provision if anyone wishes to dispute the implementability issue (the onus remaining on Stelco). My decision today re: implementability should in no way be taken as deciding any corporate reorganization issue or anything of that or related nature. I therefore sanction and approve the Plan.

J.M. Farley

DATE: January 20, 2006

TAB 4

Re Canadian Airlines Corporation, 2000 ABQB 442

Date: 20000627

Action No. 0001-05071

IN THE COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL DISTRICT OF CALGARY

IN THE MATTER OF IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED;

AND IN THE MATTER OF THE *BUSINESS CORPORATIONS ACT* (ALBERTA) S.A. 1981, c. B-15, AS AMENDED, SECTION 185

AND IN THE MATTER OF CANADIAN AIRLINES CORPORATION AND CANADIAN AIRLINES INTERNATIONAL LTD.

REASONS FOR DECISION
of the
HONOURABLE MADAM JUSTICE M. S. PAPERNY

I. INTRODUCTION

[1] After a decade of searching for a permanent solution to its ongoing, significant financial problems, Canadian Airlines Corporation ("CAC") and Canadian Airlines International Ltd. ("CAIL") seek the court's sanction to a plan of arrangement filed under the ***Companies' Creditors Arrangement Act*** ("CCAA") and sponsored by its historic rival, Air Canada Corporation ("Air Canada"). To Canadian, this represents its last choice and its only chance for survival. To Air Canada, it is an opportunity to lead the restructuring of the Canadian airline industry, an exercise many suggest is long overdue. To over 16,000 employees of Canadian, it means continued employment. Canadian Airlines will operate as a separate entity and continue to provide domestic and international air service to Canadians. Tickets of the flying public will be honoured and their frequent flyer points maintained. Long term business relationships with trade creditors and suppliers will continue.

[2] The proposed restructuring comes at a cost. Secured and unsecured creditors are being asked to accept significant compromises and shareholders of CAC are being asked to accept that their shares have no value. Certain unsecured creditors oppose the plan, alleging it is oppressive and unfair. They assert that Air Canada has appropriated the key assets of Canadian to itself. Minority shareholders of CAC, on the other hand, argue that Air Canada's financial support to Canadian, before and during this restructuring process, has increased the value of Canadian and in turn their shares. These two positions are irreconcilable, but do reflect the perception by some that this plan asks them to sacrifice too much.

[3] Canadian has asked this court to sanction its plan under s. 6 of the CCAA. The court's role on a sanction hearing is to consider whether the plan fairly balances the interests of all the stakeholders. Faced with an insolvent organization, its role is to look forward and ask: does this plan represent a fair and reasonable compromise that will permit a viable commercial entity to emerge? It is also an exercise in assessing current reality by comparing available commercial alternatives to what is offered in the proposed plan.

II. BACKGROUND

Canadian Airlines and its Subsidiaries

[4] CAC and CAIL are corporations incorporated or continued under the ***Business Corporations Act*** of Alberta, S.A. 1981, c. B-15 ("ABCA"). 82% of CAC's shares are held by 853350 Alberta Ltd.("853350") and the remaining 18% are held publicly. CAC, directly or indirectly, owns the majority of voting shares in and controls the other Petitioner, CAIL and these shares represent CAC's principal asset. CAIL owns or has an interest in a number of other corporations directly engaged in the airline industry or other businesses related to the airline industry, including Canadian Regional Airlines Limited ("CRAL"). Where the context requires, I will refer to CAC and CAIL jointly as "Canadian" in these reasons.

[5] In the past fifteen years, CAIL has grown from a regional carrier operating under the name Pacific Western Airlines ("PWA") to one of Canada's two major airlines. By mid-1986, Canadian Pacific Air Lines Limited ("CP Air"), had acquired the regional carriers Nordair Inc. ("Nordair") and Eastern Provincial Airways ("Eastern"). In February, 1987, PWA completed its purchase of CP Air from Canadian Pacific Limited. PWA then merged the four predecessor carriers (CP Air, Eastern, Nordair, and PWA) to form one airline, "Canadian Airlines International Ltd.", which was launched in April, 1987.

[6] By April, 1989, CAIL had acquired substantially all of the common shares of Wardair Inc. and completed the integration of CAIL and Wardair Inc. in 1990.

[7] CAIL and its subsidiaries provide international and domestic scheduled and charter air transportation for passengers and cargo. CAIL provides scheduled services to approximately 30 destinations in 11 countries. Its subsidiary, Canadian Regional Airlines (1998) Ltd. ("CRAL 98") provides scheduled services to approximately 35 destinations in Canada and the United States. Through code share agreements and marketing alliances with leading carriers, CAIL and its subsidiaries provide service to approximately 225 destinations worldwide. CAIL is also engaged in charter and cargo services and the provision of services to third parties, including aircraft overhaul and maintenance, passenger and cargo handling, flight simulator and equipment rentals, employee training programs and the sale of Canadian Plus frequent flyer points. As at December 31, 1999, CAIL operated approximately 79 aircraft.

[8] CAIL directly and indirectly employs over 16,000 persons, substantially all of whom are located in Canada. The balance of the employees are located in the United States, Europe, Asia, Australia, South America and Mexico. Approximately 88% of the active employees of CAIL are subject to collective bargaining agreements.

Events Leading up to the CCAA Proceedings

[9] Canadian's financial difficulties significantly predate these proceedings.

[10] In the early 1990s, Canadian experienced significant losses from operations and deteriorating liquidity. It completed a financial restructuring in 1994 (the "1994 Restructuring") which involved employees contributing $200,000,000 in new equity in return for receipt of entitlements to common shares. In addition, Aurora Airline Investments, Inc. ("Aurora"), a subsidiary of AMR Corporation ("AMR"), subscribed for $246,000,000 in preferred shares of CAIL. Other AMR subsidiaries entered into comprehensive services and marketing arrangements with CAIL. The governments of Canada, British Columbia and Alberta provided an aggregate of $120,000,000 in loan guarantees. Senior creditors, junior creditors and shareholders of CAC and CAIL and its subsidiaries converted approximately $712,000,000 of obligations into common shares of CAC or convertible notes issued jointly by CAC and CAIL and/or received warrants entitling the holder to purchase common shares.

[11] In the latter half of 1994, Canadian built on the improved balance sheet provided by the 1994 Restructuring, focussing on strict cost controls, capacity management and aircraft utilization. The initial results were encouraging. However, a number of factors including higher than expected fuel costs, rising interest rates, decline of the Canadian dollar, a strike by

pilots of Time Air and the temporary grounding of Inter-Canadien's ATR-42 fleet undermined this improved operational performance. In 1995, in response to additional capacity added by emerging charter carriers and Air Canada on key transcontinental routes, CAIL added additional aircraft to its fleet in an effort to regain market share. However, the addition of capacity coincided with the slow-down in the Canadian economy leading to traffic levels that were significantly below expectations. Additionally, key international routes of CAIL failed to produce anticipated results. The cumulative losses of CAIL from 1994 to 1999 totalled $771 million and from January 31, 1995 to August 12, 1999, the day prior to the issuance by the Government of Canada of an Order under Section 47 of the *Canada Transportation Act* (relaxing certain rules under the *Competition Act* to facilitate a restructuring of the airline industry and described further below), the trading price of Canadian's common shares declined from $7.90 to $1.55.

[12] Canadian's losses incurred since the 1994 Restructuring severely eroded its liquidity position. In 1996, Canadian faced an environment where the domestic air travel market saw increased capacity and aggressive price competition by two new discount carriers based in western Canada. While Canadian's traffic and load factor increased indicating a positive response to Canadian's post-restructuring business plan, yields declined. Attempts by Canadian to reduce domestic capacity were offset by additional capacity being introduced by the new discount carriers and Air Canada.

[13] The continued lack of sufficient funds from operations made it evident by late fall of 1996 that Canadian needed to take action to avoid a cash shortfall in the spring of 1997. In November 1996, Canadian announced an operational restructuring plan (the "1996 Restructuring") aimed at returning Canadian to profitability and subsequently implemented a payment deferral plan which involved a temporary moratorium on payments to certain lenders and aircraft operating lessors to provide a cash bridge until the benefits of the operational restructuring were fully implemented. Canadian was able successfully to obtain the support of its lenders and operating lessors such that the moratorium and payment deferral plan was able to proceed on a consensual basis without the requirement for any court proceedings.

[14] The objective of the 1996 Restructuring was to transform Canadian into a sustainable entity by focussing on controllable factors which targeted earnings improvements over four years. Three major initiatives were adopted: network enhancements, wage concessions as supplemented by fuel tax reductions/rebates, and overhead cost reductions.

[15] The benefits of the 1996 Restructuring were reflected in Canadian's 1997 financial results when Canadian and its subsidiaries reported a consolidated net income of $5.4 million, the best results in 9 years.

[16] In early 1998, building on its 1997 results, Canadian took advantage of a strong market for U.S. public debt financing in the first half of 1998 by issuing U.S. $175,000,000 of senior secured notes in April, 1998 ("Senior Secured Notes") and U.S. $100,000,000 of unsecured notes in August, 1998 ("Unsecured Notes").

[17] The benefits of the 1996 Restructuring continued in 1998 but were not sufficient to offset a number of new factors which had a significant negative impact on financial

performance, particularly in the fourth quarter. Canadian's eroded capital base gave it limited capacity to withstand negative effects on traffic and revenue. These factors included lower than expected operating revenues resulting from a continued weakness of the Asian economies, vigorous competition in Canadian's key western Canada and the western U.S. transborder markets, significant price discounting in most domestic markets following a labour disruption at Air Canada and CAIL's temporary loss of the ability to code-share with American Airlines on certain transborder flights due to a pilot dispute at American Airlines. Canadian also had increased operating expenses primarily due to the deterioration of the value of the Canadian dollar and additional airport and navigational fees imposed by NAV Canada which were not recoverable by Canadian through fare increases because of competitive pressures. This resulted in Canadian and its subsidiaries reporting a consolidated loss of $137.6 million for 1998.

[18] As a result of these continuing weak financial results, Canadian undertook a number of additional strategic initiatives including entering the **oneworldTM** Alliance, the introduction of its new "Proud Wings" corporate image, a restructuring of CAIL 's Vancouver hub, the sale and leaseback of certain aircraft, expanded code sharing arrangements and the implementation of a service charge in an effort to recover a portion of the costs relating to NAV Canada fees.

[19] Beginning in late 1998 and continuing into 1999, Canadian tried to access equity markets to strengthen its balance sheet. In January, 1999, the Board of Directors of CAC determined that while Canadian needed to obtain additional equity capital, an equity infusion alone would not address the fundamental structural problems in the domestic air transportation market.

[20] Canadian believes that its financial performance was and is reflective of structural problems in the Canadian airline industry, most significantly, over capacity in the domestic air transportation market. It is the view of Canadian and Air Canada that Canada's relatively small population and the geographic distribution of that population is unable to support the overlapping networks of two full service national carriers. As described further below, the Government of Canada has recognized this fundamental problem and has been instrumental in attempts to develop a solution.

Initial Discussions with Air Canada

[21] Accordingly, in January, 1999, CAC's Board of Directors directed management to explore all strategic alternatives available to Canadian, including discussions regarding a possible merger or other transaction involving Air Canada.

[22] Canadian had discussions with Air Canada in early 1999. AMR also participated in those discussions. While several alternative merger transactions were considered in the course of these discussions, Canadian, AMR and Air Canada were unable to reach agreement.

[23] Following the termination of merger discussions between Canadian and Air Canada, senior management of Canadian, at the direction of the Board and with the support of AMR, renewed its efforts to secure financial partners with the objective of obtaining either an equity

investment and support for an eventual merger with Air Canada or immediate financial support for a merger with Air Canada.

Offer by Onex

[24] In early May, the discussions with Air Canada having failed, Canadian focussed its efforts on discussions with Onex Corporation ("Onex") and AMR concerning the basis upon which a merger of Canadian and Air Canada could be accomplished.

[25] On August 23, 1999, Canadian entered into an Arrangement Agreement with Onex, AMR and Airline Industry Revitalization Co. Inc. ("AirCo") (a company owned jointly by Onex and AMR and controlled by Onex). The Arrangement Agreement set out the terms of a Plan of Arrangement providing for the purchase by AirCo of all of the outstanding common and non-voting shares of CAC. The Arrangement Agreement was conditional upon, among other things, the successful completion of a simultaneous offer by AirCo for all of the voting and non-voting shares of Air Canada. On August 24, 1999, AirCo announced its offers to purchase the shares of both CAC and Air Canada and to subsequently merge the operations of the two airlines to create one international carrier in Canada.

[26] On or about September 20, 1999 the Board of Directors of Air Canada recommended against the AirCo offer. On or about October 19, 1999, Air Canada announced its own proposal to its shareholders to repurchase shares of Air Canada. Air Canada's announcement also indicated Air Canada's intention to make a bid for CAC and to proceed to complete a merger with Canadian subject to a restructuring of Canadian's debt.

[27] There were several rounds of offers and counter-offers between AirCo and Air Canada. On November 5, 1999, the Quebec Superior Court ruled that the AirCo offer for Air Canada violated the provisions of the *Air Canada Public Participation Act*. AirCo immediately withdrew its offers. At that time, Air Canada indicated its intention to proceed with its offer for CAC.

[28] Following the withdrawal of the AirCo offer to purchase CAC, and notwithstanding Air Canada's stated intention to proceed with its offer, there was a renewed uncertainty about Canadian's future which adversely affected operations. As described further below, Canadian lost significant forward bookings which further reduced the company's remaining liquidity.

Offer by 853350

[29] On November 11, 1999, 853350 (a corporation financed by Air Canada and owned as to 10% by Air Canada) made a formal offer for all of the common and non-voting shares of CAC. Air Canada indicated that the involvement of 853350 in the take-over bid was necessary in order to protect Air Canada from the potential adverse effects of a restructuring of Canadian's debt and that Air Canada would only complete a merger with Canadian after the completion of a debt restructuring transaction. The offer by 853350 was conditional upon, among other things, a satisfactory resolution of AMR's claims in respect of Canadian and a satisfactory resolution of certain regulatory issues arising from the announcement made on

October 26, 1999 by the Government of Canada regarding its intentions to alter the regime governing the airline industry.

[30] As noted above, AMR and its subsidiaries and affiliates had certain agreements with Canadian arising from AMR's investment (through its wholly owned subsidiary, Aurora Airline Investments, Inc.) in CAIL during the 1994 Restructuring. In particular, the Services Agreement by which AMR and its subsidiaries and affiliates provided certain reservations, scheduling and other airline related services to Canadian provided for a termination fee of approximately $500 million (as at December 31, 1999) while the terms governing the preferred shares issued to Aurora provided for exchange rights which were only retractable by Canadian upon payment of a redemption fee in excess of $500 million (as at December 31, 1999). Unless such provisions were amended or waived, it was practically impossible for Canadian to complete a merger with Air Canada since the cost of proceeding without AMR's consent was simply too high.

[31] Canadian had continued its efforts to seek out all possible solutions to its structural problems following the withdrawal of the AirCo offer on November 5, 1999. While AMR indicated its willingness to provide a measure of support by allowing a deferral of some of the fees payable to AMR under the Services Agreement, Canadian was unable to find any investor willing to provide the liquidity necessary to keep Canadian operating while alternative solutions were sought.

[32] After 853350 made its offer, 853350 and Air Canada entered into discussions with AMR regarding the purchase by 853350 of AMR's shareholding in CAIL as well as other matters regarding code sharing agreements and various services provided to Canadian by AMR and its subsidiaries and affiliates. The parties reached an agreement on November 22, 1999 pursuant to which AMR agreed to reduce its potential damages claim for termination of the Services Agreement by approximately 88%.

[33] On December 4, 1999, CAC's Board recommended acceptance of 853350's offer to its shareholders and on December 21, 1999, two days before the offer closed, 853350 received approval for the offer from the Competition Bureau as well as clarification from the Government of Canada on the proposed regulatory framework for the Canadian airline industry.

[34] As noted above, Canadian's financial condition deteriorated further after the collapse of the AirCo Arrangement transaction. In particular:

a) the doubts which were publicly raised as to Canadian's ability to survive made Canadian's efforts to secure additional financing through various sale-leaseback transactions more difficult;
b) sales for future air travel were down by approximately 10% compared to 1998;
c) CAIL's liquidity position, which stood at approximately $84 million (consolidated cash and available credit) as at September 30, 1999, reached a critical point in late December, 1999 when it was about to go negative.

[35] In late December, 1999, Air Canada agreed to enter into certain transactions designed to ensure that Canadian would have enough liquidity to continue operating until the scheduled completion of the 853350 take-over bid on January 4, 2000. Air Canada agreed to purchase rights to the Toronto-Tokyo route for $25 million and to a sale-leaseback arrangement involving certain unencumbered aircraft and a flight simulator for total proceeds of approximately $20 million. These transactions gave Canadian sufficient liquidity to continue operations through the holiday period.

[36] If Air Canada had not provided the approximate $45 million injection in December 1999, Canadian would likely have had to file for bankruptcy and cease all operations before the end of the holiday travel season.

[37] On January 4, 2000, with all conditions of its offer having been satisfied or waived, 853350 purchased approximately 82% of the outstanding shares of CAC. On January 5, 1999, 853350 completed the purchase of the preferred shares of CAIL owned by Aurora. In connection with that acquisition, Canadian agreed to certain amendments to the Services Agreement reducing the amounts payable to AMR in the event of a termination of such agreement and, in addition, the unanimous shareholders agreement which gave AMR the right to require Canadian to purchase the CAIL preferred shares under certain circumstances was terminated. These arrangements had the effect of substantially reducing the obstacles to a restructuring of Canadian's debt and lease obligations and also significantly reduced the claims that AMR would be entitled to advance in such a restructuring.

[38] Despite the $45 million provided by Air Canada, Canadian's liquidity position remained poor. With January being a traditionally slow month in the airline industry, further bridge financing was required in order to ensure that Canadian would be able to operate while a debt restructuring transaction was being negotiated with creditors. Air Canada negotiated an arrangement with the Royal Bank of Canada ("Royal Bank") to purchase a participation interest in the operating credit facility made available to Canadian. As a result of this agreement, Royal Bank agreed to extend Canadian's operating credit facility from $70 million to $120 million in January, 2000 and then to $145 million in March, 2000. Canadian agreed to supplement the assignment of accounts receivable security originally securing Royal's $70 million facility with a further Security Agreement securing certain unencumbered assets of Canadian in consideration for this increased credit availability. Without the support of Air Canada or another financially sound entity, this increase in credit would not have been possible.

[39] Air Canada has stated publicly that it ultimately wishes to merge the operations of Canadian and Air Canada, subject to Canadian completing a financial restructuring so as to permit Air Canada to complete the acquisition on a financially sound basis. This pre-condition has been emphasized by Air Canada since the fall of 1999.

[40] Prior to the acquisition of majority control of CAC by 853350, Canadian's management, Board of Directors and financial advisors had considered every possible alternative for restoring Canadian to a sound financial footing. Based upon Canadian's extensive efforts over the past year in particular, but also the efforts since 1992 described

above, Canadian came to the conclusion that it must complete a debt restructuring to permit the completion of a full merger between Canadian and Air Canada.

[41] On February 1, 2000, Canadian announced a moratorium on payments to lessors and lenders. As a result of this moratorium Canadian defaulted on the payments due under its various credit facilities and aircraft leases. Absent the assistance provided by this moratorium, in addition to Air Canada's support, Canadian would not have had sufficient liquidity to continue operating until the completion of a debt restructuring.

[42] Following implementation of the moratorium, Canadian with Air Canada embarked on efforts to restructure significant obligations by consent. The further damage to public confidence which a CCAA filing could produce required Canadian to secure a substantial measure of creditor support in advance of any public filing for court protection.

[43] Before the Petitioners started these CCAA proceedings, Air Canada, CAIL and lessors of 59 aircraft in its fleet had reached agreement in principle on the restructuring plan.

[44] Canadian and Air Canada have also been able to reach agreement with the remaining affected secured creditors, being the holders of the U.S. $175 million Senior Secured Notes, due 2005, (the "Senior Secured Noteholders") and with several major unsecured creditors in addition to AMR, such as Loyalty Management Group Canada Inc.

[45] On March 24, 2000, faced with threatened proceedings by secured creditors, Canadian petitioned under the CCAA and obtained a stay of proceedings and related interim relief by Order of the Honourable Chief Justice Moore on that same date. Pursuant to that Order, PricewaterhouseCoopers, Inc. was appointed as the Monitor, and companion proceedings in the United States were authorized to be commenced.

[46] Since that time, due to the assistance of Air Canada, Canadian has been able to complete the restructuring of the remaining financial obligations governing all aircraft to be retained by Canadian for future operations. These arrangements were approved by this Honourable Court in its Orders dated April 14, 2000 and May 10, 2000, as described in further detail below under the heading "The Restructuring Plan".

[47] On April 7, 2000, this court granted an Order giving directions with respect to the filing of the plan, the calling and holding of meetings of affected creditors and related matters.

[48] On April 25, 2000 in accordance with the said Order, Canadian filed and served the plan (in its original form) and the related notices and materials.

[49] The plan was amended, in accordance with its terms, on several occasions, the form of Plan voted upon at the Creditors' Meetings on May 26, 2000 having been filed and served on May 25, 2000 (the "Plan").

The Restructuring Plan

[50] The Plan has three principal aims described by Canadian:

(a) provide near term liquidity so that Canadian can sustain operations;
(b) allow for the return of aircraft not required by Canadian; and
(c) permanently adjust Canadian's debt structure and lease facilities to reflect the current market for asset values and carrying costs in return for Air Canada providing a guarantee of the restructured obligations.

[51] The proposed treatment of stakeholders is as follows:

1. Unaffected Secured Creditors- Royal Bank, CAIL's operating lender, is an unaffected creditor with respect to its operating credit facility. Royal Bank holds security over CAIL's accounts receivable and most of CAIL's operating assets not specifically secured by aircraft financiers or the Senior Secured Noteholders. As noted above, arrangements entered into between Air Canada and Royal Bank have provided CAIL with liquidity necessary for it to continue operations since January 2000.

Also unaffected by the Plan are those aircraft lessors, conditional vendors and secured creditors holding security over CAIL's aircraft who have entered into agreements with CAIL and/or Air Canada with respect to the restructuring of CAIL's obligations. A number of such agreements, which were initially contained in the form of letters of intent ("LOIs"), were entered into prior to the commencement of the CCAA proceedings, while a total of 17 LOIs were completed after that date. In its Second and Fourth Reports the Monitor reported to the court on these agreements. The LOIs entered into after the proceedings commenced were reviewed and approved by the court on April 14, 2000 and May 10, 2000.

The basis of the LOIs with aircraft lessors was that the operating lease rates were reduced to fair market lease rates or less, and the obligations of CAIL under the leases were either assumed or guaranteed by Air Canada. Where the aircraft was subject to conditional sale agreements or other secured indebtedness, the value of the secured debt was reduced to the fair market value of the aircraft, and the interest rate payable was reduced to current market rates reflecting Air Canada's credit. CAIL's obligations under those agreements have also been assumed or guaranteed by Air Canada. The claims of these creditors for reduced principal and interest amounts, or reduced lease payments, are Affected Unsecured Claims under the Plan. In a number of cases these claims have been assigned to Air Canada and Air Canada disclosed that it would vote those claims in favour of the Plan.

2. Affected Secured Creditors- The Affected Secured Creditors under the Plan are the Senior Secured Noteholders with a claim in the amount of US$175,000,000. The Senior Secured Noteholders are secured by a diverse package of Canadian's assets, including its inventory of aircraft spare parts, ground equipment, spare engines, flight simulators, leasehold interests at Toronto, Vancouver and Calgary airports, the shares in CRAL 98 and a $53 million note payable by CRAL to CAIL.

The Plan offers the Senior Secured Noteholders payment of 97 cents on the dollar. The deficiency is included in the Affected Unsecured Creditor class and the Senior Secured Noteholders advised the court they would be voting the deficiency in favour of the Plan.

3. Unaffected Unsecured Creditors-In the circular accompanying the November 11, 1999 853350 offer it was stated that:

> The Offeror intends to conduct the Debt Restructuring in such a manner as to seek to ensure that the unionized employees of Canadian, the suppliers of new credit (including trade credit) and the members of the flying public are left unaffected.
> The Offeror is of the view that the pursuit of these three principles is essential in order to ensure that the long term value of Canadian is preserved.

Canadian's employees, customers and suppliers of goods and services are unaffected by the CCAA Order and Plan.
Also unaffected are parties to those contracts or agreements with Canadian which are not being terminated by Canadian pursuant to the terms of the March 24, 2000 Order.

4. Affected Unsecured Creditors- CAIL has identified unsecured creditors who do not fall into the above three groups and listed these as Affected Unsecured Creditors under the Plan. They are offered 14 cents on the dollar on their claims. Air Canada would fund this payment.

The Affected Unsecured Creditors fall into the following categories:

a. Claims of holders of or related to the Unsecured Notes (the "Unsecured Noteholders");
b. Claims in respect of certain outstanding or threatened litigation involving Canadian;
c. Claims arising from the termination, breach or repudiation of certain contracts, leases or agreements to which Canadian is a party other than aircraft financing or lease arrangements;
d. Claims in respect of deficiencies arising from the termination or re-negotiation of aircraft financing or lease arrangements;
e. Claims of tax authorities against Canadian; and
f. Claims in respect of the under-secured or unsecured portion of amounts due to the Senior Secured Noteholders.

[52] There are over $700 million of proven unsecured claims. Some unsecured creditors have disputed the amounts of their claims for distribution purposes. These are in the process of determination by the court-appointed Claims Officer and subject to further appeal to the court. If the Claims Officer were to allow all of the disputed claims in full and this were confirmed by the court, the aggregate of unsecured claims would be approximately $1.059 million.

[53] The Monitor has concluded that if the Plan is not approved and implemented, Canadian will not be able to continue as a going concern and in that event, the only foreseeable

alternative would be a liquidation of Canadian's assets by a receiver and/or a trustee in bankruptcy. Under the Plan, Canadian's obligations to parties essential to ongoing operations, including employees, customers, travel agents, fuel, maintenance and equipment suppliers, and airport authorities are in most cases to be treated as unaffected and paid in full. In the event of a liquidation, those parties would not, in most cases, be paid in full and, except for specific lien rights and statutory priorities, would rank as ordinary unsecured creditors. The Monitor estimates that the additional unsecured claims which would arise if Canadian were to cease operations as a going concern and be forced into liquidation would be in excess of $1.1 billion.

[54] In connection with its assessment of the Plan, the Monitor performed a liquidation analysis of CAIL as at March 31, 2000 in order to estimate the amounts that might be recovered by CAIL's creditors and shareholders in the event of disposition of CAIL's assets by a receiver or trustee. The Monitor concluded that a liquidation would result in a shortfall to certain secured creditors, including the Senior Secured Noteholders, a recovery by ordinary unsecured creditors of between one cent and three cents on the dollar, and no recovery by shareholders.

[55] There are two vociferous opponents of the Plan, Resurgence Asset Management LLC ("Resurgence") who acts on behalf of its and/or its affiliate client accounts and four shareholders of CAC. Resurgence is incorporated pursuant to the laws of New York, U.S.A. and has its head office in White Plains, New York. It conducts an investment business specializing in high yield distressed debt. Through a series of purchases of the Unsecured Notes commencing in April 1999, Resurgence clients hold $58,200,000 of the face value of or 58.2% of the notes issued. Resurgence purchased 7.9 million units in April 1999. From November 3, 1999 to December 9, 1999 it purchased an additional 20,850,000 units. From January 4, 2000 to February 3, 2000 Resurgence purchased an additional 29,450,000 units.

[56] Resurgence seeks declarations that: the actions of Canadian, Air Canada and 853350 constitute an amalgamation, consolidation or merger with or into Air Canada or a conveyance or transfer of all or substantially all of Canadian's assets to Air Canada; that any plan of arrangement involving Canadian will not affect Resurgence and directing the repurchase of their notes pursuant to the provisions of their trust indenture and that the actions of Canadian, Air Canada and 853350 are oppressive and unfairly prejudicial to it pursuant to section 234 of the Business Corporations Act.

[57] Four shareholders of CAC also oppose the plan. Neil Baker, a Toronto resident, acquired 132,500 common shares at a cost of $83,475.00 on or about May 5, 2000. Mr. Baker sought to commence proceedings to "remedy an injustice to the minority holders of the common shares". Roger Midiaty, Michael Salter and Hal Metheral are individual shareholders who were added as parties at their request during the proceedings. Mr. Midiaty resides in Calgary, Alberta and holds 827 CAC shares which he has held since 1994. Mr. Metheral is also a Calgary resident and holds approximately 14,900 CAC shares in his RRSP and has held them since approximately 1994 or 1995. Mr. Salter is a resident of Scottsdale, Arizona and is the beneficial owner of 250 shares of CAC and is a joint beneficial owner of 250 shares with his wife. These shareholders will be referred in the Decision throughout as the "Minority Shareholders".

[58] The Minority Shareholders oppose the portion of the Plan that relates to the reorganization of CAIL, pursuant to section 185 of the ***Alberta Business Corporations Act*** ("ABCA"). They characterize the transaction as a cancellation of issued shares unauthorized by section 167 of the ABCA or alternatively is a violation of section 183 of the ABCA. They submit the application for the order of reorganization should be denied as being unlawful, unfair and not supported by the evidence.

III. ANALYSIS

[59] Section 6 of the CCAA provides that:

> 6. Where a majority in number representing two-thirds in value of the creditors, or class of creditors, as the case may be, present and voting either in person or by proxy at the meeting or meetings thereof respectively held pursuant to sections 4 and 5, or either of those sections, agree to any compromise or arrangement either as proposed or as altered or modified at the meeting or meetings, the compromise or arrangement may be sanctioned by the court, and if so sanctioned is binding
>
> (a) on all the creditors or the class of creditors, as the case may be, and on any trustee for any such class of creditors, whether secured or unsecured, as the case may be, and on the company; and
> (b) in the case of a company that has made an authorized assignment or against which a receiving order has been made under the Bankruptcy and Insolvency Act or is in the course of being wound up under the Winding-up and Restructuring Act, on the trustee in bankruptcy or liquidator and contributories of the company.

[60] Prior to sanctioning a plan under the CCAA, the court must be satisfied in regard to each of the following criteria:

> (1) there must be compliance with all statutory requirements;
> (2) all material filed and procedures carried out must be examined to determine if anything has been done or purported to be done which is not authorized by the CCAA; and
> (3) the plan must be fair and reasonable.

[61] A leading articulation of this three-part test appears in ***Re Northland Properties Ltd.*** (1988), 73 C.B.R. (N.S.) 175 (B.C.S.C.) at 182-3, aff'd (1989), 73 C.B.R. (N.S.) 195 (B.C.C.A.) and has been regularly followed, see for example ***Re Sammi Atlas Inc.*** (1998), 3 C.B.R. (4th) 171 (Ont. Gen. Div.) at 172 and ***Re T. Eaton Co.***, [1999] O.J. No. 5322 (Ont. Sup. Ct.) at paragraph 7. Each of these criteria are reviewed in turn below.

1. Statutory Requirements

[62] Some of the matters that may be considered by the court on an application for approval of a plan of compromise and arrangement include:

> (a) the applicant comes within the definition of "debtor company" in section 2 of the CCAA;

(b) the applicant or affiliated debtor companies have total claims within the meaning of section 12 of the CCAA in excess of $5,000,000;
(c) the notice calling the meeting was sent in accordance with the order of the court;
(d) the creditors were properly classified;
(e) the meetings of creditors were properly constituted;
(f) the voting was properly carried out; and
(g) the plan was approved by the requisite double majority or majorities.

[63] I find that the Petitioners have complied with all applicable statutory requirements. Specifically:

(a) CAC and CAIL are insolvent and thus each is a "debtor company" within the meaning of section 2 of the CCAA. This was established in the affidavit evidence of Douglas Carty, Senior Vice President and Chief Financial Officer of Canadian, and so declared in the March 24, 2000 Order in these proceedings and confirmed in the testimony given by Mr. Carty at this hearing.

(b) CAC and CAIL have total claims that would be claims provable in bankruptcy within the meaning of section 12 of the CCAA in excess of $5,000,000.

(c) In accordance with the April 7, 2000 Order of this court, a Notice of Meeting and a disclosure statement (which included copies of the Plan and the March 24th and April 7th Orders of this court) were sent to the Affected Creditors, the directors and officers of the Petitioners, the Monitor and persons who had served a Notice of Appearance, on April 25, 2000.

(d) As confirmed by the May 12, 2000 ruling of this court (leave to appeal denied May 29, 2000), the creditors have been properly classified.

(e) Further, as detailed in the Monitor's Fifth Report to the Court and confirmed by the June 14, 2000 decision of this court in respect of a challenge by Resurgence Asset Management LLC ("Resurgence"), the meetings of creditors were properly constituted, the voting was properly carried out and the Plan was approved by the requisite double majorities in each class. The composition of the majority of the unsecured creditor class is addressed below under the heading "Fair and Reasonable".

2. Matters Unauthorized

[64] This criterion has not been widely discussed in the reported cases. As recognized by Blair J. in ***Olympia & York Developments Ltd.* v. *Royal Trust Co.*** (1993), 17 C.B.R. (3d) 1 (Ont. Gen. Div.) and Farley J. in ***Cadillac Fairview (Re)*** (1995), 53 A.C.W.S. (3d) 305 (Ont. Gen. Div.), within the CCAA process the court must rely on the reports of the Monitor as well as the parties in ensuring nothing contrary to the CCAA has occurred or is contemplated by the plan.

[65] In this proceeding, the dissenting groups have raised two matters which in their view are unauthorized by the CCAA: firstly, the Minority Shareholders of CAC suggested the proposed share capital reorganization of CAIL is illegal under the ABCA and Ontario

Securities Commission Policy 9.1, and as such cannot be authorized under the CCAA and secondly, certain unsecured creditors suggested that the form of release contained in the Plan goes beyond the scope of release permitted under the CCAA.

a. Legality of proposed share capital reorganization

[66] Subsection 185(2) of the ABCA provides:

> (2) If a corporation is subject to an order for reorganization, its articles may be amended by the order to effect any change that might lawfully be made by an amendment under section 167.

[67] Sections 6.1(2)(d) and (e) and Schedule "D" of the Plan contemplate that:

> a. All CAIL common shares held by CAC will be converted into a single retractable share, which will then be retracted by CAIL for $1.00; and
> b. All CAIL preferred shares held by 853350 will be converted into CAIL common shares.

[68] The Articles of Reorganization in Schedule "D" to the Plan provide for the following amendments to CAIL's Articles of Incorporation to effect the proposed reorganization:

> (a) consolidating all of the issued and outstanding common shares into one common share;
> (b) redesignating the existing common shares as "Retractable Shares" and changing the rights, privileges, restrictions and conditions attaching to the Retractable Shares so that the Retractable Shares shall have attached thereto the rights, privileges, restrictions and conditions as set out in the Schedule of Share Capital;
> (c) cancelling the Non-Voting Shares in the capital of the corporation, none of which are currently issued and outstanding, so that the corporation is no longer authorized to issue Non-Voting Shares;
> (d) changing all of the issued and outstanding Class B Preferred Shares of the corporation into Class A Preferred Shares, on the basis of one (1) Class A Preferred Share for each one (1) Class B Preferred Share presently issued and outstanding;
> (e) redesignating the existing Class A Preferred Shares as "Common Shares" and changing the rights, privileges, restrictions and conditions attaching to the Common Shares so that the Common Shares shall have attached thereto the rights, privileges, restrictions and conditions as set out in the Schedule of Share Capital; and
> (f) cancelling the Class B Preferred Shares in the capital of the corporation, none of which are issued and outstanding after the change in paragraph (d) above, so that the corporation is no longer authorized to issue Class B Preferred Shares;

Section 167 of the ABCA

[69] Reorganizations under section 185 of the ABCA are subject to two preconditions:
a. The corporation must be "subject to an order for re-organization"; and
b. The proposed amendments must otherwise be permitted under section 167 of the ABCA.

[70] The parties agreed that an order of this court sanctioning the Plan would satisfy the first condition.

[71] The relevant portions of section 167 provide as follows:

> 167(1) Subject to sections 170 and 171, the articles of a corporation may by special resolution be amended to
> (e) change the designation of all or any of its shares, and add, change or remove any rights, privileges, restrictions and conditions, including rights to accrued dividends, in respect of all or any of its shares, whether issued or unissued,
> (f) change the shares of any class or series, whether issued or unissued, into a different number of shares of the same class or series into the same or a different number of shares of other classes or series,
> (g.1) cancel a class or series of shares where there are no issued or outstanding shares of that class or series,

[72] Each change in the proposed CAIL Articles of Reorganization corresponds to changes permitted under s. 167(1) of the ABCA, as follows:

Proposed Amendment in Schedule "D"	Subsection 167(1), ABCA
(a) – consolidation of Common Shares	167(1)(f)
(b) – change of designation and rights	167(1)(e)
(c) – cancellation	167(1)(g.1)
(d) – change in shares	167(1)(f)
(e) – change of designation and rights	167(1)(e)
(f) – cancellation	167(1)(g.1)

[73] The Minority Shareholders suggested that the proposed reorganization effectively cancels their shares in CAC. As the above review of the proposed reorganization demonstrates, that is not the case. Rather, the shares of CAIL are being consolidated, altered and then retracted, as permitted under section 167 of the ABCA. I find the proposed reorganization of CAIL's share capital under the Plan does not violate section 167.

[74] In R. Dickerson et al, ***Proposals for a New Business Corporation Law for Canada,*** Vol.1: Commentary (the "Dickerson Report") regarding the then proposed Canada Business Corporations Act, the identical section to section 185 is described as having been inserted with the object of enabling the "court to effect any necessary amendment of the articles of the corporation in order to achieve the objective of the reorganization without having to comply with the formalities ~~of the Draft Act, particularly shareholder approval of the proposed~~ amendment".

[75] The architects of the business corporation act model which the ABCA follows, expressly contemplated reorganizations in which the insolvent corporation would eliminate the interest of common shareholders. The example given in the Dickerson Report of a reorganization is very similar to that proposed in the Plan:

> For example, the reorganization of an insolvent corporation may require the following steps: first, reduction or even elimination of the interest of the common shareholders; second, relegation of the preferred shareholders to the status of common shareholders; and third, relegation of the secured debenture holders to the status of either unsecured Noteholders or preferred shareholders.

[76] The rationale for allowing such a reorganization appears plain; the corporation is insolvent, which means that on liquidation the shareholders would get nothing. In those circumstances, as described further below under the heading "Fair and Reasonable", there is nothing unfair or unreasonable in the court effecting changes in such situations without shareholder approval. Indeed, it would be unfair to the creditors and other stakeholders to permit the shareholders (whose interest has the lowest priority) to have any ability to block a reorganization.

[77] The Petitioners were unable to provide any case law addressing the use of section 185 as proposed under the Plan. They relied upon the decisions of ***Royal Oak Mines Inc.***, [1999] O.J. No. 4848 and ***Re T Eaton Co.,*** *supra* in which Farley J.of the Ontario Superior Court of Justice emphasized that shareholders are at the bottom of the hierarchy of interests in liquidation or liquidation related scenarios.

[78] Section 185 provides for amendment to articles by court order. I see no requirement in that section for a meeting or vote of shareholders of CAIL, quite apart from shareholders of CAC. Further, dissent and appraisal rights are expressly removed in subsection (7). To require a meeting and vote of shareholders and to grant dissent and appraisal rights in circumstances of insolvency would frustrate the object of section 185 as described in the Dickerson Report.

[79] In the circumstances of this case, where the majority shareholder holds 82% of the shares, the requirement of a special resolution is meaningless. To require a vote suggests the shares have value. They do not. The formalities of the ABCA serve no useful purpose other than to frustrate the reorganization to the detriment of all stakeholders, contrary to the CCAA.

Section 183 of the ABCA

[80] The Minority Shareholders argued in the alternative that if the proposed share reorganization of CAIL were not a cancellation of their shares in CAC and therefore allowed under section 167 of the ABCA, it constituted a "sale, lease, or exchange of substantially all the property" of CAC and thus required the approval of CAC shareholders pursuant to section 183 of the ABCA. The Minority Shareholders suggested that the common shares in CAIL were substantially all of the assets of CAC and that all of those shares were being "exchanged" for $1.00.

[81] I disagree with this creative characterization. The proposed transaction is a reorganization as contemplated by section 185 of the ABCA. As recognized in ***Savage v.***

Amoco Acquisition Company Ltd, [1988] A.J. No. 68 (Q.B.), aff'd, 68 C.B.R. (3d) 154 (Alta. C.A.), the fact that the same end might be achieved under another section does not exclude the section to be relied on. A statute may well offer several alternatives to achieve a similar end.

Ontario Securities Commission Policy 9.1

[82] The Minority Shareholders also submitted the proposed reorganization constitutes a "related party transaction" under Policy 9.1 of the Ontario Securities Commission. Under the Policy, transactions are subject to disclosure, minority approval and formal valuation requirements which have not been followed here. The Minority Shareholders suggested that the Petitioners were therefore in breach of the Policy unless and until such time as the court is advised of the relevant requirements of the Policy and grants its approval as provided by the Policy.

[83] These shareholders asserted that in the absence of evidence of the going concern value of CAIL so as to determine whether that value exceeds the rights of the Preferred Shares of CAIL, the Court should not waive compliance with the Policy.

[84] To the extent that this reorganization can be considered a "related party transaction", I have found, for the reasons discussed below under the heading "Fair and Reasonable", that the Plan, including the proposed reorganization, is fair and reasonable and accordingly I would waive the requirements of Policy 9.1.

b. Release

[85] Resurgence argued that the release of directors and other third parties contained in the Plan does not comply with the provisions of the CCAA.

[86] The release is contained in section 6.2(2)(ii) of the Plan and states as follows:

> As of the Effective Date, each of the Affected Creditors will be deemed to forever release, waive and discharge all claims, obligations, suits, judgments, damages, demands, debts, rights, causes of action and liabilities...that are based in whole or in part on any act, omission, transaction, event or other occurrence taking place on or prior to the Effective Date in any way relating to the Applicants and Subsidiaries, the CCAA Proceedings, or the Plan against:(i) The Applicants and Subsidiaries; (ii) The Directors, Officers and employees of the Applicants or Subsidiaries in each case as of the date of filing (and in addition, those who became Officers and/or Directors thereafter but prior to the Effective Date); (iii) The former Directors, Officers and employees of the Applicants or Subsidiaries, or (iv) the respective current and former professionals of the entities in subclauses (1) to (3) of this s.6.2(2) (including, for greater certainty, the Monitor, its counsel and its current Officers and Directors, and current and former Officers, Directors, employees, shareholders and professionals of the released parties) acting in such capacity.

[87] Prior to 1997, the CCAA did not provide for compromises of claims against anyone other than the petitioning company. In 1997, section 5.1 was added to the CCAA. Section 5.1 states:

> 5.1 (1) A compromise or arrangement made in respect of a debtor company may include in its terms provision for the compromise of claims against directors of the company that arose before the commencement of proceedings under this Act and relate to the obligations of the company where the directors are by law liable in their capacity as directors for the payment of such obligations.
>
> (2) A provision for the compromise of claims against directors may not include claims that:
>
> (a) relate to contractual rights of one or more creditors; or
>
> (b) are based on allegations of misrepresentations made by directors to creditors or of wrongful or oppressive conduct by directors.
>
> (3) The Court may declare that a claim against directors shall not be compromised if it is satisfied that the compromise would not be fair and reasonable in the circumstances.

[88] Resurgence argued that the form of release does not comply with section 5.1 of the CCAA insofar as it applies to individuals beyond directors and to a broad spectrum of claims beyond obligations of the Petitioners for which their directors are "by law liable". Resurgence submitted that the addition of section 5.1 to the CCAA constituted an exception to a long standing principle and urged the court to therefore interpret s. 5.1 cautiously, if not narrowly. Resurgence relied on ***Barrette v. Crabtree Estate,*** [1993], 1 S.C.R. 1027 at 1044 and ***Bruce Agra Foods Limited v. Proposal of Everfresh Beverages Inc. (Receiver of)*** (1996), 45 C.B.R. (3d) 169 (Ont. Gen. Div.) at para. 5 in this regard.

[89] With respect to Resurgence's complaint regarding the breadth of the claims covered by the release, the Petitioners asserted that the release is not intended to override section 5.1(2). Canadian suggested this can be expressly incorporated into the form of release by adding the words **"excluding the claims excepted by s. 5.1(2) of the CCAA"** immediately prior to subsection (iii) and clarifying the language in Section 5.1 of the Plan. Canadian also acknowledged, in response to a concern raised by Canada Customs and Revenue Agency, that in accordance with s. 5.1(1) of the CCAA, directors of CAC and CAIL could only be released from liability arising before March 24, 2000, the date these proceedings commenced. Canadian suggested this was also addressed in the proposed amendment. Canadian did not address the propriety of including individuals in addition to directors in the form of release.

[90] In my view it is appropriate to amend the proposed release to expressly comply with section 5. 1(2) of the CCAA and to clarify Section 5.1 of the Plan as Canadian suggested in its brief. The additional language suggested by Canadian to achieve this result shall be included in the form of order. Canada Customs and Revenue Agency is apparently satisfied with the Petitioners' acknowledgement that claims against directors can only be released to the date of commencement of proceedings under the CCAA, having appeared at this hearing to strongly support the sanctioning of the Plan, so I will not address this concern further.

[91] Resurgence argued that its claims fell within the categories of excepted claims in section 5.1(2) of the CCAA and accordingly, its concern in this regard is removed by this amendment. Unsecured creditors JHHD Aircraft Leasing No. 1 and No. 2 suggested there may be possible wrongdoing in the acts of the directors during the restructuring process which should not be immune from scrutiny and in my view this complaint would also be caught by the exception captured in the amendment.

[92] While it is true that section 5.2 of the CCAA does not authorize a release of claims against third parties other than directors, it does not prohibit such releases either. The amended terms of the release will not prevent claims from which the CCAA expressly prohibits release. Aside from the complaints of Resurgence, which by their own submissions are addressed in the amendment I have directed, and the complaints of JHHD Aircraft Leasing No. 1 and No. 2, which would also be addressed in the amendment, the terms of the release have been accepted by the requisite majority of creditors and I am loathe to further disturb the terms of the Plan, with one exception.

[93] Amex Bank of Canada submitted that the form of release appeared overly broad and might compromise unaffected claims of affected creditors. For further clarification, Amex Bank of Canada's potential claim for defamation is unaffected by the Plan and I am prepared to order Section 6.2(2)(ii) be amended to reflect this specific exception.

3. Fair and Reasonable

[94] In determining whether to sanction a plan of arrangement under the CCAA, the court is guided by two fundamental concepts: "fairness" and "reasonableness". While these concepts are always at the heart of the court's exercise of its discretion, their meanings are necessarily shaped by the unique circumstances of each case, within the context of the Act and accordingly can be difficult to distill and challenging to apply. Blair J. described these concepts in ***Olympia and York Dev. Ltd. v. Royal Trust Co.***, *supra*, at page 9:

> "Fairness" and "reasonableness" are, in my opinion, the two keynote concepts underscoring the philosophy and workings of the Companies' Creditors Arrangement Act. Fairness is the quintessential expression of the court's equitable jurisdiction - although the jurisdiction is statutory, the broad discretionary powers given to the judiciary by the legislation which make its exercise an exercise in equity - and "reasonableness" is what lends objectivity to the process.

[95] The legislation, while conferring broad discretion on the court, offers little guidance. However, the court is assisted in the exercise of its discretion by the purpose of the CCAA: to facilitate the reorganization of a debtor company for the benefit of the company, its creditors, shareholders, employees and, in many instances, a much broader constituency of affected persons. Parliament has recognized that reorganization, if commercially feasible, is in most cases preferable, economically and socially, to liquidation: ***Norcen Energy Resources Ltd.* v. *Oakwood Petroleums Ltd.***, [1989] 2 W.W.R. 566 at 574 (Alta.Q.B.); ***Northland Properties Ltd.* v. *Excelsior Life Insurance Co. of Canada***, [1989] 3 W.W.R. 363 at 368 (B.C.C.A.).

[96] The sanction of the court of a creditor-approved plan is not to be considered as a rubber stamp process. Although the majority vote that brings the plan to a sanction hearing plays a significant role in the court's assessment, the court will consider other matters as are appropriate in light of its discretion. In the unique circumstances of this case, it is appropriate to consider a number of additional matters:

a. The composition of the unsecured vote;
b. What creditors would receive on liquidation or bankruptcy as compared to the Plan;
c. Alternatives available to the Plan and bankruptcy;
d. Oppression;
e. Unfairness to Shareholders of CAC; and
f. The public interest.

a. Composition of the unsecured vote

[97] As noted above, an important measure of whether a plan is fair and reasonable is the parties' approval and the degree to which it has been given. Creditor support creates an inference that the plan is fair and reasonable because the assenting creditors believe that their interests are treated equitably under the plan. Moreover, it creates an inference that the arrangement is economically feasible and therefore reasonable because the creditors are in a better position then the courts to gauge business risk. As stated by Blair J. at page 11 of ***Olympia & York Developments Ltd.***, *supra:*

> As other courts have done, I observe that it is not my function to second guess the business people with respect to the "business" aspect of the Plan or descending into the negotiating arena or substituting my own view of what is a fair and reasonable compromise or arrangement for that of the business judgment of the participants. The parties themselves know best what is in their interests in those areas.

[98] However, given the manner of voting under the CCAA, the court must be cognizant of the treatment of minorities within a class: see for example ***Quintette Coal Ltd.,*** (1992) 13 C.B.R. (3rd) 14 (B.C.S.C) and ***Re Alabama, New Orleans, Texas and Pacific Junction Railway Co.*** (1890) 60 L.J. Ch. 221 (C.A.). The court can address this by ensuring creditors' claims are properly classified. As well, it is sometimes appropriate to tabulate the vote of a particular class so the results can be assessed from a fairness perspective. In this case, the classification was challenged by Resurgence and I dismissed that application. The vote was also tabulated in this case and the results demonstrate that the votes of Air Canada and the Senior Secured Noteholders, who voted their deficiency in the unsecured class, were decisive.

[99] The results of the unsecured vote, as reported by the Monitor, are:

1. For the resolution to approve the Plan: 73 votes (65% in number) representing $494,762,304 in claims (76% in value);
2. Against the resolution: 39 votes (35% in number) representing $156,360,363 in claims (24% in value); and
3. Abstentions: 15 representing $968,036 in value.

[100] The voting results as reported by the Monitor were challenged by Resurgence. That application was dismissed.

[101] The members of each class that vote in favour of a plan must do so in good faith and the majority within a class must act without coercion in their conduct toward the minority. When asked to assess fairness of an approved plan, the court will not countenance secret agreements to vote in favour of a plan secured by advantages to the creditor: see for example, ***Hochberger* v. *Rittenberg*** (1916), 36 D.L.R. 450 (S.C.C.)

[102] ***In Northland Properties Ltd. (Re)*** (1988), 73 C.B.R. (N.S.) 175 at 192-3 (B.C.S.C) aff'd 73 C.B.R. (N.S.) 195 (B.C.C.A.), dissenting priority mortgagees argued the plan violated the principle of equality due to an agreement between the debtor company and another priority mortgagee which essentially amounted to a preference in exchange for voting in favour of the plan. Trainor J. found that the agreement was freely disclosed and commercially reasonable and went on to approve the plan, using the three part test. The British Columbia Court of Appeal upheld this result and in commenting on the minority complaint McEachern J.A. stated at page 206:

> In my view, the obvious benefits of settling rights and keeping the enterprise together as a going concern far outweigh the deprivation of the appellants' wholly illusory rights. In this connection, the learned chambers judge said at p.29:
>
> > I turn to the question of the right to hold the property after an order absolute and whether or not this is a denial of something of that significance that it should affect these proceedings. There is in the material before me some evidence of values. There are the principles to which I have referred, as well as to the rights of majorities and the rights of minorities.
> > Certainly, those minority rights are there, but it would seem to me that in view of the overall plan, in view of the speculative nature of holding property in the light of appraisals which have been given as to value, that this right is something which should be subsumed to the benefit of the majority.

[103] Resurgence submitted that Air Canada manipulated the indebtedness of CAIL to assure itself of an affirmative vote. I disagree. I previously ruled on the validity of the deficiency when approving the LOIs and found the deficiency to be valid. I found there was consideration for the assignment of the deficiency claims of the various aircraft financiers to Air Canada, namely the provision of an Air Canada guarantee which would otherwise not have been available until plan sanction. The Monitor reviewed the calculations of the deficiencies and determined they were calculated in a reasonable manner. As such, the court approved those transactions. If the deficiency had instead remained with the aircraft financiers, it is reasonable to assume those claims would have been voted in favour of the plan. Further, it would have been entirely appropriate under the circumstances for the aircraft financiers to have retained the deficiency and agreed to vote in favour of the Plan, with the same result to Resurgence. That the financiers did not choose this method was explained by the testimony of Mr. Carty and Robert Peterson, Chief Financial Officer for Air Canada; quite simply it amounted to a desire on behalf of these creditors to shift the "deal risk" associated with the Plan to Air Canada. The agreement reached with the Senior Secured Noteholders was also disclosed and the challenge by Resurgence regarding their vote in the unsecured class was dismissed There

is nothing inappropriate in the voting of the deficiency claims of Air Canada or the Senior Secured Noteholders in the unsecured class. There is no evidence of secret vote buying such as discussed in ***Northland Properties Ltd. (Re)***.

[104] If the Plan is approved, Air Canada stands to profit in its operation. I do not accept that the deficiency claims were devised to dominate the vote of the unsecured creditor class, however, Air Canada, as funder of the Plan is more motivated than Resurgence to support it. This divergence of views on its own does not amount to bad faith on the part of Air Canada. Resurgence submitted that only the Unsecured Noteholders received 14 cents on the dollar. That is not accurate, as demonstrated by the list of affected unsecured creditors included earlier in these Reasons. The Senior Secured Noteholders did receive other consideration under the Plan, but to suggest they were differently motivated suggests that those creditors did not ascribe any value to their unsecured claims. There is no evidence to support this submission.

[105] The good faith of Resurgence in its vote must also be considered. Resurgence acquired a substantial amount of its claim after the failure of the Onex bid, when it was aware that Canadian's financial condition was rapidly deteriorating. Thereafter, Resurgence continued to purchase a substantial amount of this highly distressed debt. While Mr. Symington maintained that he bought because he thought the bonds were a good investment, he also acknowledged that one basis for purchasing was the hope of obtaining a blocking position sufficient to veto a plan in the proposed debt restructuring. This was an obvious ploy for leverage with the Plan proponents

[106] The authorities which address minority creditors' complaints speak of "substantial injustice" (***Keddy Motor Inns Ltd. (Re)*** (1992) 13 C.B.R. (3d) 245 (N.S.C.A.), "confiscation" of rights (***Campeau Corp. (Re)*** (1992), 10 C.B.R. (3d) 104 (Ont. Ct. (Gen.Div.); ***Skydome Corp. (Re)*** (1999), 87 A.C.W.S (3d) 421 (Ont. Ct. Gen. Div.)) and majorities "feasting upon" the rights of the minority (***Quintette Coal Ltd. (Re)***, (1992), 13 C.B.R.(3d) 146 (B.C.S.C.). Although it cannot be disputed that the group of Unsecured Noteholders represented by Resurgence are being asked to accept a significant reduction of their claims, as are all of the affected unsecured creditors, I do not see a "substantial injustice", nor view their rights as having been "confiscated" or "feasted upon" by being required to succumb to the wishes of the majority in their class. No bad faith has been demonstrated in this case. Rather, the treatment of Resurgence, along with all other affected unsecured creditors, represents a reasonable balancing of interests. While the court is directed to consider whether there is an injustice being worked within a class, it must also determine whether there is an injustice with respect the stakeholders as a whole. Even if a plan might at first blush appear to have that effect, when viewed in relation to all other parties, it may nonetheless be considered appropriate and be approved: ***Algoma Steel Corp.* v. *Royal Bank*** (1992), 11 C.B.R. (3d) 1 (Ont. Gen. Div.)and ***Northland Properties (Re)***, *supra* at 9.

[107] Further, to the extent that greater or discrete motivation to support a Plan may be seen as a conflict, the Court should take this same approach and look at the creditors as a whole and to the objecting creditors specifically and determine if their rights are compromised in an attempt to balance interests and have the pain of compromise borne equally.

[108] Resurgence represents 58.2% of the Unsecured Noteholders or $96 million in claims. The total claim of the Unsecured Noteholders ranges from $146 million to $161 million. The

affected unsecured class, excluding aircraft financing, tax claims, the noteholders and claims under $50,000, ranges from $116.3 million to $449.7 million depending on the resolutions of certain claims by the Claims Officer. Resurgence represents between 15.7% - 35% of that portion of the class.

[109] The total affected unsecured claims, excluding tax claims, but including aircraft financing and noteholder claims including the unsecured portion of the Senior Secured Notes, ranges from $673 million to $1,007 million. Resurgence represents between 9.5% - 14.3% of the total affected unsecured creditor pool. These percentages indicate that at its very highest in a class excluding Air Canada's assigned claims and Senior Secured's deficiency, Resurgence would only represent a maximum of 35% of the class. In the larger class of affected unsecured it is significantly less. Viewed in relation to the class as a whole, there is no injustice being worked against Resurgence.

[110] The thrust of the Resurgence submissions suggests a mistaken belief that they will get more than 14 cents on liquidation. This is not borne out by the evidence and is not reasonable in the context of the overall Plan.

b. Receipts on liquidation or bankruptcy

[111] As noted above, the Monitor prepared and circulated a report on the Plan which contained a summary of a liquidation analysis outlining the Monitor's projected realizations upon a liquidation of CAIL ("Liquidation Analysis").

[112] The Liquidation Analysis was based on: (1) the draft unaudited financial statements of Canadian at March 31, 2000; (2) the distress values reported in independent appraisals of aircraft and aircraft related assets obtained by CAIL in January, 2000; (3) a review of CAIL's aircraft leasing and financing documents; and (4) discussions with CAIL Management.

[113] Prior to and during the application for sanction, the Monitor responded to various requests for information by parties involved. In particular, the Monitor provided a copy of the Liquidation Analysis to those who requested it. Certain of the parties involved requested the opportunity to question the Monitor further, particularly in respect to the Liquidation Analysis and this court directed a process for the posing of those questions.

[114] While there were numerous questions to which the Monitor was asked to respond, there were several areas in which Resurgence and the Minority Shareholders took particular issue: pension plan surplus, CRAL, international routes and tax pools. The dissenting groups asserted that these assets represented overlooked value to the company on a liquidation basis or on a going concern basis.

Pension Plan Surplus

[115] The Monitor did not attribute any value to pension plan surplus when it prepared the Liquidation Analysis, for the following reasons:

1) The summaries of the solvency surplus/deficit positions indicated a cumulative net deficit position for the seven registered plans, after consideration of contingent liabilities;
2) The possibility, based on the previous splitting out of the seven plans from a single plan in 1988, that the plans could be held to be consolidated for financial purposes, which would remove any potential solvency surplus since the total estimated contingent liabilities exceeded the total estimated solvency surplus;
3) The actual calculations were prepared by CAIL's actuaries and actuaries representing the unions could conclude liabilities were greater; and
4) CAIL did not have a legal opinion confirming that surpluses belonged to CAIL.

[116] The Monitor concluded that the entitlement question would most probably have to be settled by negotiation and/or litigation by the parties. For those reasons, the Monitor took a conservative view and did not attribute an asset value to pension plans in the Liquidation Analysis. The Monitor also did not include in the Liquidation Analysis any amount in respect of the claim that could be made by members of the plan where there is an apparent deficit after deducting contingent liabilities.

[117] The issues in connection with possible pension surplus are: (1) the true amount of any of the available surplus; and (2) the entitlement of Canadian to any such amount.

[118] It is acknowledged that surplus prior to termination can be accessed through employer contribution holidays, which Canadian has taken to the full extent permitted. However, there is no basis that has been established for any surplus being available to be withdrawn from an ongoing pension plan. On a pension plan termination, the amount available as a solvency surplus would first have to be further reduced by various amounts to determine whether there was in fact any true surplus available for distribution. Such reductions include contingent benefits payable in accordance with the provisions of each respective pension plan, any extraordinary plan wind up cost, the amounts of any contribution holidays taken which have not been reflected, and any litigation costs.

[119] Counsel for all of Canadian's unionized employees confirmed on the record that the respective union representatives can be expected to dispute all of these calculations as well as to dispute entitlement.

[120] There is a suggestion that there might be a total of $40 million of surplus remaining from all pension plans after such reductions are taken into account. Apart from the issue of entitlement, this assumes that the plans can be treated separately, that a surplus could in fact be realized on liquidation and that the Towers Perrin calculations are not challenged. With total pension plan assets of over $2 billion, a surplus of $40 million could quickly disappear with relatively minor changes in the market value of the securities held or calculation of liabilities. In the circumstances, given all the variables, I find that the existence of any surplus is doubtful at best and I am satisfied that the Monitor's Liquidation Analysis ascribing it zero value is reasonable in this circumstances.

CRAL

[121] The Monitor's liquidation analysis as at March 31, 2000 of CRAL determined that in a distress situation, after payments were made to its creditors, there would be a deficiency of approximately $30 million to pay Canadian Regional's unsecured creditors, which include a claim of approximately $56.5 million due to Canadian. In arriving at this conclusion, the Monitor reviewed internally prepared unaudited financial statements of CRAL as of March 31, 2000, the Houlihan Lokey Howard and Zukin, distress valuation dated January 21, 2000 and the Simat Helliesen and Eichner valuation of selected CAIL assets dated January 31, 2000 for certain aircraft related materials and engines, rotables and spares. The Avitas Inc., and Avmark Inc. reports were used for the distress values on CRAL's aircraft and the CRAL aircraft lease documentation. The Monitor also performed its own analysis of CRAL's liquidation value, which involved analysis of the reports provided and details of its analysis were outlined in the Liquidation Analysis.

[122] For the purpose of the Liquidation Analysis, the Monitor did not consider other airlines as comparable for evaluation purposes, as the Monitor's valuation was performed on a distressed sale basis. The Monitor further assumed that without CAIL's national and international network to feed traffic into and a source of standby financing, and considering the inevitable negative publicity which a failure of CAIL would produce, CRAL would immediately stop operations as well.

[123] Mr. Peterson testified that CRAL was worth $260 million to Air Canada, based on Air Canada being a special buyer who could integrate CRAL, on a going concern basis, into its network. The Liquidation Analysis assumed the windup of each of CRAL and CAIL, a completely different scenario.

[124] There is no evidence that there was a potential purchaser for CRAL who would be prepared to acquire CRAL or the operations of CRAL 98 for any significant sum or at all. CRAL has value to CAIL, and in turn, could provide value to Air Canada, but this value is attributable to its ability to feed traffic to and take traffic from the national and international service operated by CAIL. In my view, the Monitor was aware of these features and properly considered these factors in assessing the value of CRAL on a liquidation of CAIL.

[125] If CAIL were to cease operations, the evidence is clear that CRAL would be obliged to do so as well immediately. The travelling public, shippers, trade suppliers, and others would make no distinction between CAIL and CRAL and there would be no going concern for Air Canada to acquire.

International Routes

[126] The Monitor ascribed no value to Canadian's international routes in the Liquidation Analysis. In discussions with CAIL management and experts available in its aviation group, the Monitor was advised that international routes are unassignable licenses and not property rights. They do not appear as assets in CAIL's financials. Mr. Carty and Mr. Peterson explained that routes and slots are <u>not</u> treated as assets by airlines, but rather as rights in the control of the Government of Canada. In the event of bankruptcy/receivership of CAIL, CAIL's trustee/receiver could not sell them and accordingly they are of no value to CAIL.

[127] Evidence was led that on June 23, 1999 Air Canada made an offer to purchase CAIL's international routes for $400 million cash plus $125 million for aircraft spares and inventory, along with the assumption of certain debt and lease obligations for the aircraft required for the international routes. CAIL evaluated the Air Canada offer and concluded that the proposed purchase price was insufficient to permit it to continue carrying on business in the absence of its international routes. Mr. Carty testified that something in the range of $2 billion would be required.

[128] CAIL was in desperate need of cash in mid December, 1999. CAIL agreed to sell its Toronto - Tokyo route for $25 million. The evidence, however, indicated that the price for the Toronto - Tokyo route was not derived from a valuation, but rather was what CAIL asked for, based on its then-current cash flow requirements. Air Canada and CAIL obtained Government approval for the transfer on December 21, 2000.

[129] Resurgence complained that despite this evidence of offers for purchase and actual sales of international routes and other evidence of sales of slots, the Monitor did not include Canadian's international routes in the Liquidation Analysis and only attributed a total of $66 million for all intangibles of Canadian. There is some evidence that slots at some foreign airports may be bought or sold in some fashion. However, there is insufficient evidence to attribute any value to other slots which CAIL has at foreign airports. It would appear given the regulation of the airline industry, in particular, the ***Aeronautics Act*** and the ***Canada Transportation Act***, that international routes for a Canadian air carrier only have full value to the extent of federal government support for the transfer or sale, and its preparedness to allow the then-current license holder to sell rather than act unilaterally to change the designation. The federal government was prepared to allow CAIL to sell its Toronto - Tokyo route to Air Canada in light of CAIL's severe financial difficulty and the certainty of cessation of operations during the Christmas holiday season in the absence of such a sale.

[130] Further, statements made by CAIL in mid-1999 as to the value of its international routes and operations in response to an offer by Air Canada, reflected the amount CAIL needed to sustain liquidity without its international routes and was not a representation of market value of what could realistically be obtained from an arms length purchaser. The Monitor concluded on its investigation that CAIL's Narida and Heathrow slots had a realizable value of $66 million , which it included in the Liquidation Analysis. I find that this conclusion is supportable and that the Monitor properly concluded that there were no other rights which ought to have been assigned value.

Tax Pools

[131] There are four tax pools identified by Resurgence and the Minority Shareholders that are material: capital losses at the CAC level, undepreciated capital cost pools, operating losses incurred by Canadian and potential for losses to be reinstated upon repayment of fuel tax rebates by CAIL.

Capital Loss Pools

[132] The capital loss pools at CAC will not be available to Air Canada since CAC is to be left out of the corporate reorganization and will be severed from CAIL. Those capital losses

can essentially only be used to absorb a portion of the debt forgiveness liability associated with the restructuring. CAC, who has virtually all of its senior debt compromised in the plan, receives compensation for this small advantage, which cost them nothing.

Undepreciated capital cost ("UCC")

[133] There is no benefit to Air Canada in the pools of UCC unless it were established that the UCC pools are in excess of the fair market value of the relevant assets, since Air Canada could create the same pools by simply buying the assets on a liquidation at fair market value. Mr. Peterson understood this pool of UCC to be approximately $700 million . There is no evidence that the UCC pool, however, could be considered to be a source of benefit. There is no evidence that this amount is any greater than fair market value.

Operating Losses

[134] The third tax pool complained of is the operating losses. The debt forgiven as a result of the Plan will erase any operating losses from prior years to the extent of such forgiven debt.

Fuel tax rebates

[135] The fourth tax pool relates to the fuel tax rebates system taken advantage of by CAIL in past years. The evidence is that on a consolidated basis the total potential amount of this pool is $297 million. According to Mr. Carty's testimony, CAIL has not been taxable in his ten years as Chief Financial Officer. The losses which it has generated for tax purposes have been sold on a 10 - 1 basis to the government in order to receive rebates of excise tax paid for fuel. The losses can be restored retroactively if the rebates are repaid, but the losses can only be carried forward for a maximum of seven years. The evidence of Mr. Peterson indicates that Air Canada has no plan to use those alleged losses and in order for them to be useful to Air Canada, Air Canada would have to complete a legal merger with CAIL, which is not provided for in the plan and is not contemplated by Air Canada until some uncertain future date. In my view, the Monitor's conclusion that there was no value to any tax pools in the Liquidation Analysis is sound.

[136] Those opposed to the Plan have raised the spectre that there may be value unaccounted for in this liquidation analysis or otherwise. Given the findings above, this is merely speculation and is unsupported by any concrete evidence.

c. Alternatives to the Plan

[137] When presented with a plan, affected stakeholders must weigh their options in the light of commercial reality. Those options are typically liquidation measured against the plan proposed. If not put forward, a hope for a different or more favourable plan is not an option and no basis upon which to assess fairness. On a purposive approach to the CCAA, what is fair and reasonable must be assessed against the effect of the Plan on the creditors and their various claims, in the context of their response to the plan. Stakeholders are expected to decide their fate based on realistic, commercially viable alternatives (generally seen as the prime motivating factor in any business decision) and not on speculative desires or hope for the

future. As Farley J. stated in ***Re T. Eaton Co.*** (1999) O.J. No. 4216 (Ont. Sup. Ct.) at paragraph 6:

> One has to be cognizant of the function of a balancing of their prejudices. Positions must be realistically assessed and weighed, all in the light of what an alternative to a successful plan would be. Wishes are not a firm foundation on which to build a plan; nor are ransom demands.

[138] The evidence is overwhelming that all other options have been exhausted and have resulted in failure. The concern of those opposed suggests that there is a better plan that Air Canada can put forward. I note that significant enhancements were made to the plan during the process. In any case, this is the Plan that has been voted on. The evidence makes it clear that there is not another plan forthcoming. As noted by Farley J. in ***T. Eaton Co***, *supra*, "no one presented an alternative plan for the interested parties to vote on" (para. 8).

d. Oppression

Oppression and the CCAA

[139] Resurgence and the Minority Shareholders originally claimed that the Plan proponents, CAC and CAIL and the Plan supporters 853350 and Air Canada had oppressed, unfairly disregarded or unfairly prejudiced their interests, under Section 234 of the ABCA. The Minority Shareholders (for reasons that will appear obvious) have abandoned that position.

[140] Section 234 gives the court wide discretion to remedy corporate conduct that is unfair. As remedial legislation, it attempts to balance the interests of shareholders, creditors and management to ensure adequate investor protection and maximum management flexibility. The Act requires the court to judge the conduct of the company and the majority in the context of equity and fairness: ***First Edmonton Place Ltd. v. 315888 Alberta Ltd.***, (1988) 40 B.L.R.28 (Alta. Q.B.). Equity and fairness are measured against or considered in the context of the rights, interests or reasonable expectations of the complainants: ***Re Diligenti v. RWMD Operations Kelowna*** (1976), 1 B.C.L.R. 36 (S.C).

[141] The starting point in any determination of oppression requires an understanding as to what the rights, interests, and reasonable expectations are and what the damaging or detrimental effect is on them. MacDonald J. stated in ***First Edmonton Place***, *supra* at 57:

> In deciding what is unfair, the history and nature of the corporation, the essential nature of the relationship between the corporation and the creditor, the type of rights affected in general commercial practice should all be material. More concretely, the test of unfair prejudice or unfair disregard should encompass the following considerations: The protection of the underlying expectation of a creditor in the arrangement with the corporation, the extent to which the acts complained of were unforeseeable where the creditor could not reasonably have protected itself from such acts and the detriment to the interests of the creditor.

[142] While expectations vary considerably with the size, structure, and value of the corporation, all expectations must be reasonably and objectively assessed: ***Pente Investment Management Ltd. v. Schneider Corp.*** (1998), 42 O.R. (3d) 177 (C.A.).

[143] Where a company is insolvent, only the creditors maintain a meaningful stake in its assets. Through the mechanism of liquidation or insolvency legislation, the interests of shareholders are pushed to the bottom rung of the priority ladder. The expectations of creditors and shareholders must be viewed and measured against an altered financial and legal landscape. Shareholders cannot reasonably expect to maintain a financial interest in an insolvent company where creditors' claims are not being paid in full. It is through the lens of insolvency that the court must consider whether the acts of the company are in fact oppressive, unfairly prejudicial or unfairly disregarded. CCAA proceedings have recognized that shareholders may not have "a true interest to be protected" because there is no reasonable prospect of economic value to be realized by the shareholders given the existing financial misfortunes of the company: ***Re Royal Oak Mines Ltd.***, *supra*, para. 4., ***Re Cadillac Fairview***, [1995] O.J. 707 (Ont. Sup. Ct), and ***Re T. Eaton Company,*** *supra.*

[144] To avail itself of the protection of the CCAA, a company must be insolvent. The CCAA considers the hierarchy of interests and assesses fairness and reasonableness in that context. The court's mandate not to sanction a plan in the absence of fairness necessitates the determination as to whether the complaints of dissenting creditors and shareholders are legitimate, bearing in mind the company's financial state. The articulated purpose of the Act and the jurisprudence interpreting it, "widens the lens" to balance a broader range of interests that includes creditors and shareholders and beyond to the company, the employees and the public, and tests the fairness of the plan with reference to its impact on all of the constituents.

[145] It is through the lens of insolvency legislation that the rights and interests of both shareholders and creditors must be considered. The reduction or elimination of rights of both groups is a function of the insolvency and not of oppressive conduct in the operation of the CCAA. The antithesis of oppression is fairness, the guiding test for judicial sanction. If a plan unfairly disregards or is unfairly prejudicial it will not be approved. However, the court retains the power to compromise or prejudice rights to effect a broader purpose, the restructuring of an insolvent company, provided that the plan does so in a fair manner.

Oppression allegations by Resurgence

[146] Resurgence alleges that it has been oppressed or had its rights disregarded because the Petitioners and Air Canada disregarded the specific provisions of their trust indenture, that Air Canada and 853350 dealt with other creditors outside of the CCAA, refusing to negotiate with Resurgence and that they are generally being treated inequitably under the Plan.

[147] The trust indenture under which the Unsecured Notes were issued required that upon a "change of control", 101% of the principal owing thereunder, plus interest would be immediately due and payable. Resurgence alleges that Air Canada, through 853350, caused CAC and CAIL to purposely fail to honour this term. Canadian acknowledges that the trust indenture was breached. On February 1, 2000, Canadian announced a moratorium on payments to lessors and lenders, including the Unsecured Noteholders. As a result of this

moratorium, Canadian defaulted on the payments due under its various credit facilities and aircraft leases.

[148] The moratorium was not directed solely at the Unsecured Noteholders. It had the same impact on other creditors, secured and unsecured. Canadian, as a result of the moratorium, breached other contractual relationships with various creditors. The breach of contract is not sufficient to found a claim for oppression in this case. Given Canadian's insolvency, which Resurgence recognized, it cannot be said that there was a reasonable expectation that it would be paid in full under the terms of the trust indenture, particularly when Canadian had ceased making payments to other creditors as well.

[149] It is asserted that because the Plan proponents engaged in a restructuring of Canadian's debt before the filing under the CCAA, that its use of the Act for only a small group of creditors, which includes Resurgence is somehow oppressive.

[150] At the outset, it cannot be overlooked that the CCAA does not require that a compromise be proposed to all creditors of an insolvent company. The CCAA is a flexible, remedial statute which recognizes the unique circumstances that lead to and away from insolvency.

[151] Next, Air Canada made it clear beginning in the fall of 1999 that Canadian would have to complete a financial restructuring so as to permit Air Canada to acquire CAIL on a financially sound basis and as a wholly owned subsidiary. Following the implementation of the moratorium, absent which Canadian could not have continued to operate, Canadian and Air Canada commenced efforts to restructure significant obligations by consent. They perceived that further damage to public confidence that a CCAA filing could produce, required Canadian to secure a substantial measure of creditor support in advance of any public filing for court protection. Before the Petitioners started the CCAA proceedings on March 24, 2000, Air Canada, CAIL and lessors of 59 aircraft in its fleet had reached agreement in principle on the restructuring plan.

[152] The purpose of the CCAA is to create an environment for negotiations and compromise. Often it is the stay of proceedings that creates the necessary stability for that process to unfold. Negotiations with certain key creditors in advance of the CCAA filing, rather than being oppressive or conspiratorial, are to be encouraged as a matter of principle if their impact is to provide a firm foundation for a restructuring. Certainly in this case, they were of critical importance, staving off liquidation, preserving cash flow and allowing the Plan to proceed. Rather than being detrimental or prejudicial to the interests of the other stakeholders, including Resurgence, it was beneficial to Canadian and all of its stakeholders.

[153] Resurgence complained that certain transfers of assets to Air Canada and its actions in consolidating the operations of the two entities prior to the initiation of the CCAA proceedings were unfairly prejudicial to it.

[154] The evidence demonstrates that the sales of the Toronto - Tokyo route, the Dash 8s and the simulators were at the suggestion of Canadian, who was in desperate need of operating cash. Air Canada paid what Canadian asked, based on its cash flow requirements. The

evidence established that absent the injection of cash at that critical juncture, Canadian would have ceased operations. It is for that reason that the Government of Canada willingly provided the approval for the transfer on December 21, 2000.

[155] Similarly, the renegotiation of CAIL's aircraft leases to reflect market rates supported by Air Canada covenant or guarantee has been previously dealt with by this court and found to have been in the best interest of Canadian, not to its detriment. The evidence establishes that the financial support and corporate integration that has been provided by Air Canada was not only in Canadian's best interest, but its only option for survival. The suggestion that the renegotiations of these leases, various sales and the operational realignment represents an assumption of a benefit by Air Canada to the detriment of Canadian is not supported by the evidence.

[156] I find the transactions predating the CCAA proceedings, were in fact Canadian's life blood in ensuring some degree of liquidity and stability within which to conduct an orderly restructuring of its debt. There was no detriment to Canadian or to its creditors, including its unsecured creditors. That Air Canada and Canadian were so successful in negotiating agreements with their major creditors, including aircraft financiers, without resorting to a stay under the CCAA underscores the serious distress Canadian was in and its lenders recognition of the viability of the proposed Plan.

[157] Resurgence complained that other significant groups held negotiations with Canadian. The evidence indicates that a meeting was held with Mr. Symington, Managing Director of Resurgence, in Toronto in March 2000. It was made clear to Resurgence that the pool of unsecured creditors would be somewhere between $500 and $700 million and that Resurgence would be included within that class. To the extent that the versions of this meeting differ, I prefer and accept the evidence of Mr. Carty. Resurgence wished to play a significant role in the debt restructuring and indicated it was prepared to utilize the litigation process to achieve a satisfactory result for itself. It is therefore understandable that no further negotiations took place. Nevertheless, the original offer to affected unsecured creditors has been enhanced since the filing of the plan on April 25, 2000. The enhancements to unsecured claims involved the removal of the cap on the unsecured pool and an increase from 12 to 14 cents on the dollar.

[158] The findings of the Commissioner of Competition establishes beyond doubt that absent the financial support provided by Air Canada, Canadian would have failed in December 1999. I am unable to find on the evidence that Resurgence has been oppressed. The complaint that Air Canada has plundered Canadian and robbed it of its assets is not supported but contradicted by the evidence. As described above, the alternative is liquidation and in that event the Unsecured Noteholders would receive between one and three cents on the dollar. The Monitor's conclusions in this regard are supportable and I accept them.

e. Unfairness to Shareholders

[159] The Minority Shareholders essentially complained that they were being unfairly stripped of their only asset in CAC - the shares of CAIL. They suggested they were being squeezed out by the new CAC majority shareholder 853350, without any compensation or any

vote. When the reorganization is completed as contemplated by the Plan , their shares will remain in CAC but CAC will be a bare shell.

[160] They further submitted that Air Canada's cash infusion, the covenants and guarantees it has offered to aircraft financiers, and the operational changes (including integration of schedules, "quick win" strategies, and code sharing) have all added significant value to CAIL to the benefit of its stakeholders, including the Minority Shareholders. They argued that they should be entitled to continue to participate into the future and that such an expectation is legitimate and consistent with the statements and actions of Air Canada in regard to integration. By acting to realign the airlines before a corporate reorganization, the Minority Shareholders asserted that Air Canada has created the expectation that it is prepared to consolidate the airlines with the participation of a minority. The Minority Shareholders take no position with respect to the debt restructuring under the CCAA, but ask the court to sever the corporate reorganization provisions contained in the Plan.

[161] Finally, they asserted that CAIL has increased in value due to Air Canada's financial contributions and operational changes and that accordingly, before authorizing the transfer of the CAIL shares to 853350, the current holders of the CAIL Preferred Shares, the court must have evidence before it to justify a transfer of 100% of the equity of CAIL to the Preferred Shares.

[162] That CAC will have its shareholding in CAIL extinguished and emerge a bare shell is acknowledged. However, the evidence makes it abundantly clear that those shares, CAC's "only asset", have no value. That the Minority Shareholders are content to have the debt restructuring proceed suggests by implication that they do not dispute the insolvency of both Petitioners, CAC and CAIL.

[163] The Minority Shareholders base their expectation to remain as shareholders on the actions of Air Canada in acquiring only 82% of the CAC shares before integrating certain of the airlines' operations. Mr. Baker (who purchased <u>after</u> the Plan was filed with the Court and almost six months after the take over bid by Air Canada) suggested that the contents of the bid circular misrepresented Air Canada's future intentions to its shareholders. The two dollar price offered and paid per share in the bid must be viewed somewhat skeptically and in the context in which the bid arose. It does not support the speculative view that some shareholders hold, that somehow, despite insolvency, their shares have some value on a going concern basis. In any event, any claim for misrepresentation that Minority Shareholders might have arising from the take over bid circular against Air Canada or 853350 , if any, is unaffected by the Plan and may be pursued after the stay is lifted.

[164] In considering Resurgence's claim of oppression I have already found that the financial support of Air Canada during this restructuring period has benefited Canadian and its stakeholders. Air Canada's financial support and the integration of the two airlines has been critical to keeping Canadian afloat. The evidence makes it abundantly clear that without this support Canadian would have ceased operations. However it has not transformed CAIL or CAC into solvent companies.

[165] The Minority Shareholders raise concerns about assets that are ascribed limited or no value in the Monitor's report as does Resurgence (although to support an opposite proposition). Considerable argument was directed to the future operational savings and profitability forecasted for Air Canada, its subsidiaries and CAIL and its subsidiaries. Mr. Peterson estimated it to be in the order of $650 to $800 million on an annual basis, commencing in 2001. The Minority Shareholders point to the tax pools of a restructured company that they submit will be of great value once CAIL becomes profitable as anticipated. They point to a pension surplus that at the very least has value by virtue of the contribution holidays that it affords. They also look to the value of the compromised claims of the restructuring itself which they submit are in the order of $449 million. They submit these cumulative benefits add value, currently or at least realizable in the future. In sharp contrast to the Resurgence position that these acts constitute oppressive behaviour, the Minority Shareholders view them as enhancing the value of their shares. They go so far as to suggest that there may well be a current going concern value of the CAC shares that has been conveniently ignored or unquantified and that the Petitioners must put evidence before the court as to what that value is.

[166] These arguments overlook several important facts, the most significant being that CAC and CAIL are insolvent and will remain insolvent until the debt restructuring is fully implemented. These companies are not just technically or temporarily insolvent, they are massively insolvent. Air Canada will have invested upward of $3 billion to complete the restructuring, while the Minority Shareholders have contributed nothing. Further, it was a fundamental condition of Air Canada's support of this Plan that it become the sole owner of CAIL. It has been suggested by some that Air Canada's share purchase at two dollars per share in December 1999 was unfairly prejudicial to CAC and CAIL's creditors. Objectively, any expectation by Minority Shareholders that they should be able to participate in a restructured CAIL is not reasonable.

[167] The Minority Shareholders asserted the plan is unfair because the effect of the reorganization is to extinguish the common shares of CAIL held by CAC and to convert the voting and non-voting Preferred Shares of CAIL into common shares of CAIL. They submit there is no expert valuation or other evidence to justify the transfer of CAIL's equity to the Preferred Shares. There is no equity in the CAIL shares to transfer. The year end financials show CAIL's shareholder equity at a deficit of $790 million. The Preferred Shares have a liquidation preference of $347 million. There is no evidence to suggest that Air Canada's interim support has rendered either of these companies solvent, it has simply permitted operations to continue. In fact, the unaudited consolidated financial statements of CAC for the quarter ended March 31, 2000 show total shareholders equity went from a deficit of $790 million to a deficit of $1.214 million, an erosion of $424 million.

[168] The Minority Shareholders' submission attempts to compare and contrast the rights and expectations of the CAIL preferred shares as against the CAC common shares. This is not a meaningful exercise; the Petitioners are not submitting that the Preferred Shares have value and the evidence demonstrates unequivocally that they do not. The Preferred Shares are merely being utilized as a corporate vehicle to allow CAIL to become a wholly owned subsidiary of Air Canada. For example, the same result could have been achieved by issuing new shares rather than changing the designation of 853350's Preferred Shares in CAIL.

[169] The Minority Shareholders have asked the court to sever the reorganization from the debt restructuring, to permit them to participate in whatever future benefit might be derived from the restructured CAIL. However, a fundamental condition of this Plan and the expressed intention of Air Canada on numerous occasions is that CAIL become a wholly owned subsidiary. To suggest the court ought to sever this reorganization from the debt restructuring fails to account for the fact that it is not two plans but an integral part of a single plan. To accede to this request would create an injustice to creditors whose claims are being seriously compromised, and doom the entire Plan to failure. Quite simply, the Plan's funder will not support a severed plan.

[170] Finally, the future profits to be derived by Air Canada are not a relevant consideration. While the object of any plan under the CCAA is to create a viable emerging entity, the germane issue is what a prospective purchaser is prepared to pay in the circumstances. Here, we have the one and only offer on the table, Canadian's last and only chance. The evidence demonstrates this offer is preferable to those who have a remaining interest to a liquidation. Where secured creditors have compromised their claims and unsecured creditors are accepting 14 cents on the dollar in a potential pool of unsecured claims totalling possibly in excess of $1 billion , it is not unfair that shareholders receive nothing.

e. The Public Interest

[171] In this case, the court cannot limit its assessment of fairness to how the Plan affects the direct participants. The business of the Petitioners as a national and international airline employing over 16,000 people must be taken into account.

[172] In his often cited article, ***Reorganizations Under the Companies' Creditors Arrangement Act*** (1947), 25 Can.Bar R.ev. 587 at 593 Stanley Edwards stated:

> Another reason which is usually operative in favour of reorganization is the interest of the public in the continuation of the enterprise, particularly if the company supplies commodities or services that are necessary or desirable to large numbers of consumers, or if it employs large numbers of workers who would be thrown out of employment by its liquidation. This public interest may be reflected in the decisions of the creditors and shareholders of the company and is undoubtedly a factor which a court would wish to consider in deciding whether to sanction an arrangement under the C.C.A.A.

[173] In ***Re Repap British Columbia Inc.*** (1998), 1 C.B.R. 449 (B.C.S.C.) the court noted that the fairness of the plan must be measured against the overall economic and business environment and against the interests of the citizens of British Columbia who are affected as "shareholders" of the company, and creditors, of suppliers, employees and competitors of the company. The court approved the plan even though it was unable to conclude that it was necessarily fair and reasonable. In ***Re Quintette Coal Ltd.,*** *supra*, Thackray J. acknowledged the significance of the coal mine to the British Columbia economy, its importance to the people who lived and worked in the region and to the employees of the company and their families. Other cases in which the court considered the public interest in determining whether to sanction a plan under the CCAA include ***Canadian Red Cross Society (Re)***, (1998),5

C.B.R.(4th) (Ont. Gen. Div.) and ***Algoma Steel Corp. v. Royal Bank of Canada (Trustee of)***, [1992] O.J. No. 795 (Ont. Gen. Div.)

[174] The economic and social impacts of a plan are important and legitimate considerations. Even in insolvency, companies are more than just assets and liabilities. The fate of a company is inextricably tied to those who depend on it in various ways. It is difficult to imagine a case where the economic and social impacts of a liquidation could be more catastrophic. It would undoubtedly be felt by Canadian air travellers across the country. The effect would not be a mere ripple, but more akin to a tidal wave from coast to coast that would result in chaos to the Canadian transportation system.

[175] More than sixteen thousand unionized employees of CAIL and CRAL appeared through counsel. The unions and their membership strongly support the Plan. The unions represented included the Airline Pilots Association International, the International Association of Machinists and Aerospace Workers, Transportation District 104, Canadian Union of Public Employees, and the Canadian Auto Workers Union. They represent pilots, ground workers and cabin personnel. The unions submit that it is essential that the employee protections arising from the current restructuring of Canadian not be jeopardized by a bankruptcy, receivership or other liquidation. Liquidation would be devastating to the employees and also to the local and national economies. The unions emphasize that the Plan safeguards the employment and job dignity protection negotiated by the unions for their members. Further, the court was reminded that the unions and their members have played a key role over the last fifteen years or more in working with Canadian and responsible governments to ensure that Canadian survived and jobs were maintained.

[176] The Calgary and Edmonton Airport authorities, which are not for profit corporations, also supported the Plan. CAIL's obligations to the airport authorities are not being compromised under the Plan. However, in a liquidation scenario, the airport authorities submitted that a liquidation would have severe financial consequences to them and have potential for severe disruption in the operation of the airports.

[177] The representations of the Government of Canada are also compelling. Approximately one year ago, CAIL approached the Transport Department to inquire as to what solution could be found to salvage their ailing company. The Government saw fit to issue an order in council, pursuant to section 47 of the ***Transportation Act***, which allowed an opportunity for CAIL to approach other entities to see if a permanent solution could be found. A standing committee in the House of Commons reviewed a framework for the restructuring of the airline industry, recommendations were made and undertakings were given by Air Canada. The Government was driven by a mandate to protect consumers and promote competition. It submitted that the Plan is a major component of the industry restructuring. Bill C-26, which addresses the restructuring of the industry, has passed through the House of Commons and is presently before the Senate. The Competition Bureau has accepted that Air Canada has the only offer on the table and has worked very closely with the parties to ensure that the interests of consumers, employees, small carriers, and smaller communities will be protected.

[178] In summary, in assessing whether a plan is fair and reasonable, courts have emphasized that perfection is not required: see for example ***Wandlyn Inns Ltd. (Re)*** (1992), 15 C.B.R. (3d)

316 (N.BQ.B), ***Quintette Coal***, *supra* and ***Repap***, *supra*. Rather, various rights and remedies must be sacrificed to varying degrees to result in a reasonable, viable compromise for all concerned. The court is required to view the "big picture" of the plan and assess its impact as a whole. I return to ***Algoma Steel v. Royal Bank of Canada.***, *supra* at 9 in which Farley J. endorsed this approach:

> What might appear on the surface to be unfair to one party when viewed in relation to all other parties may be considered to be quite appropriate.

[179] Fairness and reasonableness are not abstract notions, but must be measured against the available commercial alternatives. The triggering of the statute, namely insolvency, recognizes a fundamental flaw within the company. In these imperfect circumstances there can never be a perfect plan, but rather only one that is supportable. As stated in ***Re Sammi Atlas Inc.***, (1998), 3C.B.R. (4th) 171 at 173 (Ont. Sup. Ct.) at 173:

> A plan under the CCAA is a compromise; it cannot be expected to be perfect. It should be approved if it is fair, reasonable and equitable. Equitable treatment is not necessarily equal treatment. Equal treatment may be contrary to equitable treatment.

[180] I find that in all the circumstances, the Plan is fair and reasonable.

IV. CONCLUSION

[181] The Plan has obtained the support of many affected creditors, including virtually all aircraft financiers, holders of executory contracts, AMR, Loyalty Group and the Senior Secured Noteholders.

[182] Use of these proceedings has avoided triggering more than $1.2 billion of incremental claims. These include claims of passengers with pre-paid tickets, employees, landlords and other parties with ongoing executory contracts, trade creditors and suppliers.

[183] This Plan represents a solid chance for the continued existence of Canadian. It preserves CAIL as a business entity. It maintains over 16,000 jobs. Suppliers and trade creditors are kept whole. It protects consumers and preserves the integrity of our national transportation system while we move towards a new regulatory framework. The extensive efforts by Canadian and Air Canada, the compromises made by stakeholders both within and without the proceedings and the commitment of the Government of Canada inspire confidence in a positive result.

[184] I agree with the opposing parties that the Plan is not perfect, but it is neither illegal nor oppressive. Beyond its fair and reasonable balancing of interests, the Plan is a result of bona fide efforts by all concerned and indeed is the only alternative to bankruptcy as ten years of struggle and creative attempts at restructuring by Canadian clearly demonstrate. This Plan is one step toward a new era of airline profitability that hopefully will protect consumers by promoting affordable and accessible air travel to all Canadians.

[185] The Plan deserves the sanction of this court and it is hereby granted. The application pursuant to section 185 of the ABCA is granted. The application for declarations sought by Resurgence are dismissed. The application of the Minority Shareholders is dismissed.

HEARD on the 5th day of June to the 19th day of June, 2000.
DATED at Calgary, Alberta this 27th day of June, 2000.

J.C.Q.B.A.

APPEARANCES:

A.L. Friend, Q.C.
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R.B. Low. Q.C.
L. Goldbach
For the Petitioners

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For Air Canada and 853350 Alberta Ltd.

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G. McCue
For Neil Baker, Michael Salter, Hal Metheral and Roger Midiaty

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For the Monitor, PwC

G.B. Morawetz
R.J. Chadwick
A. McConnell
For the Senior Secured Noteholders and the Bank of Nova Scotia Trust Company

C.J. Shaw, Q.C.
For the unionized employees

T. Mallett
C. Feasby
For Amex Bank of Canada

E.W. Halt
For J. Stephens Allan, Claims Officer

M. Hollins.
For Pacific Costal Airlines

P. Pastewka
For JHHD Aircraft Leasing No. 1 and No. 2

J. Thom
For the Royal Bank of Canada

J. Medhurst-Tivadar
For Canada Customs and Revenue Agency

R. Wilkins, Q.C.
For the Calgary and Edmonton Airport Authority

TAB 5

AMENDED THIS May 17/2011 PURSUANT TO
MODIFIÉ CE CONFORMÉMENT À
☐ RULE/LA RÈGLE 26.02 (   )
☐ THE ORDER OF Mr. J. Perell
L'ORDONNANCE DU
DATED / FAIT LE March 31/2011

LOCAL REGISTRAR GREFFIER LOCAL
SUPERIOR COURT OF JUSTICE COUR SUPÉRIEURE DE JUSTICE

Court File No. CV-09-378701-00CP

ONTARIO
SUPERIOR COURT OF JUSTICE

BETWEEN

ST. CLAIR PENNYFEATHER

Plaintiff

and

TIMMINCO LIMITED, PHOTON CONSULTING LLC,
ROGOL ENERGY CONSULTING LLC, MICHAEL ROGOL,
DR. HEINZ SCHIMMELBUSCH, ROBERT DIETRICH,
RENÉ BOISVERT, ARTHUR R. SPECTOR,
JACK L. MESSMAN, JOHN C. FOX, MICHAEL D. WINFIELD,
MICKEY M. YAKSICH, and JOHN P. WALSH

Defendants

Proceeding under the *Class Proceedings Act, 1992*

AMENDED STATEMENT OF CLAIM

TO THE DEFENDANTS

A LEGAL PROCEEDING HAS BEEN COMMENCED AGAINST YOU by the plaintiff. The claim made against you is set out in the following pages.

IF YOU WISH TO DEFEND THIS PROCEEDING, you or an Ontario lawyer acting for you must prepare a statement of defence in Form 18A prescribed by the Rules of Civil Procedure, serve it on the plaintiff's lawyer or, where the plaintiff does not have a lawyer, serve it on the plaintiff, and file it, with proof of service in this court office, WITHIN TWENTY DAYS after this statement of claim is served on you, if you are served in Ontario.

If you are served in another province or territory of Canada or in the United States of America, the period for serving and filing your statement of defence is forty days. If you are served outside Canada and the United States of America, the period is sixty days.

Instead of serving and filing a statement of defence, you may serve and file a notice of intent to defend in Form 18B prescribed by the Rules of Civil Procedure. This will entitle you to ten more days within which to serve and file your statement of defence.

IF YOU FAIL TO DEFEND THIS PROCEEDING, JUDGMENT MAY BE GIVEN AGAINST YOU IN YOUR ABSENCE AND WITHOUT FURTHER NOTICE TO YOU. IF YOU WISH TO DEFEND THIS PROCEEDING BUT ARE UNABLE TO PAY LEGAL FEES, LEGAL AID MAY BE AVAILABLE TO YOU BY CONTACTING A LOCAL LEGAL AID OFFICE.

IF YOU PAY THE PLAINTIFF'S CLAIM, and $5000.00 for costs, within the time for serving and filing your statement of defence you may move to have this proceeding dismissed by the court. If you believe the amount claimed for costs is excessive, you may pay the plaintiff's claim and $500.00 for costs and have the costs assessed by the court.

Date May 14/2009

Issued by S. Desouza
Local registrar

Address of Court Office:

393 University Avenue
10^{th} Floor
Toronto, ON
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TO: TIMMINCO LIMITED
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AND TO: DR. HEINZ SCHIMMELBUSCH
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AND TO: ROGOL ENGERY CONSULTING LLC
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AND TO: MICHAEL ROGOL
200 Clarendon St., 50th Floor
Boston, MA
02169

CLAIM

DEFINITIONS

1. The following definitions apply for the purpose of this Statement of Claim:

   (a) "March 2008 Press Release" means Timminco's press release dated March 17, 2008;

   (b) "March 2008 Conference Call" means the conference call conducted by Timminco with investors and analysts on March 17, 2008;

   (c) "2007 Annual Information Form" means Timminco's 2007 Annual Information Form published on SEDAR on March 28, 2008,

   (d) "2007 MD&A" means Timminco's Management's Discussion and Analysis for Fiscal Year 2007 published on SEDAR on March 28, 2008;

   (e) "2007 Annual Report" means Timminco's 2007 Annual Report published on SEDAR on March 31, 2008;

   (f) "Photon Report" means the report of Photon Consulting dated May 8, 2008;

   (g) "2008 First Quarter Results" means Timminco's first quarter results published on May 8, 2008;

   (h) "May 8, 2008 Press Release" means the two Timminco press releases dated May 8, 2008, announcing ~~the~~ Timminco's 2008 First Quarter Results and the Photon Report;

   (i) "May 8, 2008 Conference Call" means the conference call conducted by Timminco with investors and analysts on May 8, 2008;

   (j) "MD&A Q1 2008" means Timminco's Management's Discussion and Analysis for Fiscal Year 2007 and First Quarter 2008 published on SEDAR on May 13, 2008;

   (k) "May ~~13~~14, 2008 Conference Call" means the conference call conducted by Timminco with investors and analysts on May ~~13~~14, 2008; and,

   (l) "May 29, 2008 Conference Call" means the conference call conducted by Timminco with investors and analysts on May 29, 2008.

RELIEF SOUGHT

2. The Plaintiff claims on his own behalf and on behalf of the other Class Members (as defined below):

(a) an order pursuant to the *Class Proceedings Act, 1992*, S.O. 1992, c. 6, ("CPA") certifying this action as a class proceeding and appointing him as representative plaintiff;

(b) a declaration that the Defendants are liable for the Misrepresentations (as defined below) made during the Class Period (as defined below);

(c) a declaration that the Misrepresentations were made negligently;

(d) a declaration that Timminco is vicariously liable for the acts and/or omissions of the Individual Timminco Defendants (as defined below);

(e) an order allowing the Plaintiff to amend this Statement of Claim to assert the right of action provided for in Part XXIII.1 of the *Securities Act*, R.S.O. 1990, c. S.5 ("Securities Act");

(f) damages in the amount of $520,000,000.00 or such other amount as this court finds appropriate at the trial of the common issues or at a reference or references;

(g) punitive damages in the amount of $20,000,000.00;

(h) an order directing a reference or giving such other directions as may be necessary to determine issues not determined in the trial of the common issues;

(i) pre-judgement interest and post-judgement interest, compounded, or pursuant to sections 128 and 129 of the *Courts of Justice Act*, R.S.O.1990, c. C.43;

(j) costs of the action on a substantial indemnity basis or in an amount that provides full indemnity;

(k) costs of notice and of administering the plan to distribute the recovery in this action, pursuant to section 26 (9) of the CPA ~~Class Proceedings Act, 1992, S.O. 1992, c. 6, plus applicable taxes~~; and,

(l) such further and other relief as this Honourable Court deems just.

THE PLAINTIFF

~~3. The Plaintiff, Mr. Sharma, resides in the City of Richmond Hill, in the Province of Ontario. Mr. Sharma purchased shares of Timminco during the class period and suffered losses as a result of the Defendants' Misrepresentations.~~

3. The Plaintiff St. Clair Pennyfeather resides in the City of Toronto, in the Province of Ontario. Mr. Pennyfeather purchased shares of Timminco during the Class Period and suffered losses as a result of the Defendants' Misrepresentations.

THE DEFENDANTS

4. Timminco Ltd. ("Timminco") is a corporation continued under the *Canada Business Corporations Act* on July 23, 1980, which carries on the business of the production and marketing of various metals, alloys and silicon. The Company's business involves the production and marketing of solar-grade silicon for the solar photovoltaic energy industry.

5. Timminco's wholly-owned subsidiary, Bécancour Silicon Inc. ("Bécancour"), conducts Timminco's silicon production business and operates the Bécancour Plant, a solar-grade silicon production facility in Bécancour, Québec.

~~7. Photon Consulting LLC ("Photon Consulting") is a consulting firm based in Boston, MA, providing research and analysis to the solar power industry. Photon Consulting is an expert within the definition in s. 138.1 of the *Securities Act*.~~

~~8. Rogol Energy Consulting LLC ("Rogol Energy") is a consulting firm located in Boston, MA, providing research and analysis to the solar power industry. Rogol Energy is an expert within the definition in s. 138.1 of the *Securities Act*.~~

<u>6.</u> Dr. Heinz Schimmelbusch ("Schimmelbusch") is an individual resident of Pennsylvania, U.S.A., and served as Chief Executive Officer and Chairman of the Board of Directors of Timminco during the Class Period.

<u>7.</u> Robert Dietrich ("Dietrich") is an individual resident of Ontario, and served as the Executive Vice President and Chief Financial Officer of Timminco during the Class Period.

<u>8.</u> René Boisvert ("Boisvert") is an individual resident in the Province of Quebec and served as the President – Silicon of Timminco and was the President and Chief Executive Officer of Bécancour since 2004 and during the Class Period. Prior to that, Boisvert held various positions and offices with Bécancour, including President and Vice President – Operations & Technology.

~~10. Michael Regol ("Regol") is an individual resident of Boston, MA. Regol was the Managing Director of Photon Consulting and was responsible for reviewing and reporting on Timminco's operations through Photon Consulting and Regol Energy. Regol is an expert within the definition in s. 138.1 of the *Securities Act*.~~

<u>9.</u> The remaining defendants (Arthur R. Spector, Jack L. Messman, John C. Fox, Michael D. Winfield, Mickey M. Yaksich and John P. Walsh) ~~(collectively, "Directors")~~ were directors of Timminco at all material times.

<u>10.</u> By virtue of their positions as senior officers and/or directors of Timminco, ~~the individual defendants (Schimmelbusch, Dietrich and Boisvert) and Directors~~ <u>Defendants Schimmelbusch, Dietrich, Boisvert, Spector, Messman, Fox, Winfield, Yaksich and Walsh (collectively, the "Individual Timminco Defendants")</u> had actual, implied or apparent authority to act and speak on Timminco's behalf prior to and during the Class Period.

11. Michael Rogol ("Rogol") is an individual resident of Boston, MA. Rogol was the Managing Director of Photon Consulting and was responsible for reviewing and reporting on Timminco's operations through Photon Consulting LLC ("Photon Consulting") and Rogol Energy Consulting LLC ("Rogol Energy").

12. Both Photon Consulting and Rogol Energy are consulting firms located in Boston, MA, providing research and analysis to the solar power industry. Rogol, Photon Consulting and Rogol Energy (collectively, the "Photon Defendants") are experts within the definition of s. 138.1 of the *Securities Act*.

THE NATURE OF THE ACTION

13. Timminco ~~Ltd. ("Timminco" or the "Company")~~ is a publicly-traded company. Its shares trade on the Toronto Stock Exchange under the symbol TIM.

14. Until early 2007, Timminco's principal business involved the production and marketing of alloys for industrial applications. Its securities were trading at less than $1.00 per share at that time.

15. Beginning in March of 2007, Timminco announced that its wholly owned subsidiary, Bécancour ~~Silicon Inc., (Bécancour)~~, had entered into a series of commercial contracts to supply high purity silicon to solar cell manufacturers. Timminco stated that Bécancour had developed a proprietary "patent-pending process", which allowed it to produce solar-grade silicon for supply to the rapidly growing solar voltaic energy industry. Timminco announced that in response to the high demand for its product, it would begin to ramp up production by the end of 2007.

16. As is particularized below, ~~I~~In early 2008, ~~the Defendants began to describe~~ Timminco, with the authorization, permission or acquiescence of the Individual Timminco Defendants, began to issue statements that described the company as "a leader in the production and marketing of lightweight metals, specializing in solar grade silicon"~~;~~, and These statements represented that ~~it~~ Timminco was able to process "metallurgical grade silicon into low cost solar grade silicon for use in the manufacture of solar cells~~.~~" ~~The Defendants also publicly stated~~ and that Timminco had a competitive advantage over other solar-grade silicon producers because of its proprietary technology and production capabilities.

17. The Photon Defendants were experts retained by Timminco who made specific representations about the promise of Timminco's solar silicon production technology.

18. ~~As is particularized below, t~~These statements ~~by the Defendants~~ were made in press releases, conference calls, Core Documents as defined in section 138.1 of the *Securities Act* ("Core Documents"), Public Oral Statements as defined in section 138.1 of the *Securities Act* ("Public Oral Statements"), and other documents that would reasonably be expected to affect the market price of Timminco shares. The share price was artificially inflated as a result of the Defendants' misrepresentations.

19. The ~~Defendants'~~ statements affected the market price of Timminco shares between the period from March 17, 2008 through November 11, 2008 (the "Class Period").

CLASS DEFINITION

20. The Plaintiff brings this action on behalf of all persons, other than the Excluded Persons (as defined below), who acquired securities of Timminco during the Class Period ("Class Members"). The class excludes Timminco's past or present subsidiaries, officers, directors,

affiliates, legal representatives, heirs, predecessors, successors and assigns, and all members of the individual defendants' families, and any entity in which any of the individual defendants has or had a controlling interest ("Excluded Persons").

21. As particularized below, all of ~~The~~ the Defendants' ~~statements~~ made statements, or authorized, permitted or acquiesced in the release of statements, during the Class Period that Timminco had a competitive advantage in the production of solar-grade silicon, as well as released, or authorized, permitted or acquiesced in the release of statements of revenue, future estimates of production volume, margins, and profits from that business, which were materially false and misleading. All of ~~The~~ the Defendants' omissions to state during the Class Period that the Company's solar-grade silicon production process was not capable of producing silicon at quantity, cost, and purity levels consistent with Company statements, and that such problems would have detrimental effects on revenues and profits, were also materially false and misleading. Those statements and omissions (collectively, the "Misrepresentations") were misrepresentations within the meaning of s. 138.3 of the Securities Act. The Misrepresentations were made negligently and recklessly and without regard for the truth of their contents.

22. The Plaintiff seeks damages in an amount equal to the losses that he and the other Class Members suffered as a result of purchasing or acquiring Timminco securities during the Class Period.

TIMMINCO'S DISCLOSURE OBLIGATIONS

23. Timminco is a reporting issuer in Ontario and as such, pursuant to the *Securities Act*, and ~~as such Timminco~~ is:

(a) required to file on SEDAR and deliver to the Company's security holders:

(i) annual financial statements and MD&A within 90 days from the end of its last financial year, pursuant to sections 78 and 79 of the *Securities Act* and sections 4.1-4.2 and 5.1 of National Instrument 51-102, as the case may be;

(ii) quarterly interim financial statements and MD&A within 45 days of the end of each interim period pursuant to sections 4.3-4.4 and 5.1 of National Instrument 51-102; and,

(b) subject to the continuous disclosure provisions of Part XVIII of the *Securities Act* in accordance with section 1(1) of the *Securities Act*.

24. Timminco is also a "responsible issuer" in accordance with section 138.1(1) of the *Securities Act* and is therefore subject to civil liability provisions for secondary market disclosure of Part XXIII.1 of the *Securities Act*.

THE SOLAR-GRADE SILICON INDUSTRY

25. Solar cells are used to produce solar energy. The key component in solar cells is high purity silicon, called "solar-grade" silicon, defined as at least 99.999% (5-nines) pure. Ultra pure silicon (between 99.99999% or 7-nines and 99.9999999% or 9-nines pure), known as polysilicon, has been manufactured for use in the semiconductor industry for many years. This polysilicon is actually too pure for solar energy applications, and solar cell manufacturers must increase its conductivity by adding impurities, typically boron and phosphorous. The production of polysilicon requires significant capital investment and energy costs.

26. Other methods for creating solar-grade silicon exist. One of these methods involves the conversion of metallurgical silicon directly into solar-grade silicon. Although this method has been known and understood in the industry for many years, no process has yet been created whereby it can be applied on a cost-efficient commercial scale.

27. In a press release dated March 15 of 2007, Timminco announced that it had developed a process to purify chemical grade silicon to meet the specifications of solar cell industry participants.

THE MISREPRESENTATIONS DURING THE CLASS PERIOD

The March 2008 Press Release

28. On March 17, 2008, Timminco issued the March 2008 Press Release announcing its results for the fourth quarter and fiscal year ended December 31, 2007. The March 2008 Press Release is a document that would reasonably be expected to affect the market price of the shares in Timminco.

29. The March 2008 Press Release states:

> Fiscal 2007 was a year of transition for Timminco as we focused on establishing production and securing our first customer contracts in our solar-grade silicon business, while at the same time positioning our silicon metal and magnesium businesses for improved performance going forward," said Heinz Schimmelbusch, Chairman of the Board and Chief Executive Officer of Timminco. "In December, less than six months after breaking ground on our 3,600 metric ton solar-grade silicon facility, we commenced production and now have all three lines operating. Before year end, we had also secured four long-term contracts that commit us to supply up to 6,000 metric tons per year of solar-grade silicon beginning in 2009. Based on our success to date, as well as a strong pipeline of prospective customers, we made the decision last month to expand our production capacity to 14,400 metric tons annually. Looking ahead, we are firmly focused on leveraging *our position as a low-cost producer of solar-grade silicon* to capitalize on the tremendous opportunity in the high growth solar photovoltaic energy industry.

[Emphasis added]

30. The statements made in the March 2008 Press Release misrepresented that Timminco "was a low-cost producer of solar grade silicon", and further misleadingly implied that it was capable of producing solar-grade silicon with commercially acceptable impurity composition,

and of producing same at the quantity and cost as set out in the March 2008 News Release, and accordingly, these representations were ~~Misrerpesentations~~ Misrepresentations.

The March 2008 Conference Call

31. On or about March 18, 2008, Schimmelbusch conducted the March 2008 Conference Call with analysts and investors wherein he made statements relating to the business, operations and affairs of Timminco. These statements constituted Public Oral Statements, and included the following:

> In the coming years, the growth of solar energy industry is expected to experience significant growth. *We believe that we are well positioned to be a leading supplier of solar-grade silicon to solar wafer and cell manufacturers.*
>
> Early in 2007 production began at our solar-grade silicon pilot facility, and by March we had secured our first commercial contract. We followed shortly thereafter with our second contract in April.
>
> In July 2007 we broke ground on our new three-line solar-grade silicon production facility. Less than six months later, in December, our first production line was up and running, and we had secured two more sales contracts. We are now contracted to supply up to 6,000 metric tons of solar-grade silicon per year, beginning in 2009 to four key customers.
>
> In February 2008 our second line was in production, with the start of the third line by the beginning of March. Given the market acceptance of our material, several weeks ago we announced that we will further expand our annual solar-grade silicon production capacity to 14,400 metric tons. I will elaborate on this later.
>
> Purity and the composition of impurities are key specifications for the manufacture of solar cells and modules. Each [*sic*] in 2007 we achieved a purity level of five 9s, generally considered to be the minimum requirement for the manufacture of solar cells and modules.
>
> Over the course of the year we continued to improve the purity composition at this level in order to expand our base of potential customers and command higher market price. By year end we achieved an impurity composition at the 99.999% level of 0.8 parts per billion of boron and less than 5 parts per million of phosphorus, which is a significant milestone.

* * *

We are proud of our achievements in 2007 and believe that fiscal 2008 holds significant promise as we continue to build our solar-grade silicon business.

* * *

Clearly we are not satisfied with our financial performance in 2007. Looking ahead, *we see great opportunity and leverage on our solar silicon business to capitalize on high-growth opportunities.*

* * *

While we see strong prospects for our magnesium business to return to health and our aluminum wheels investments as I stated before, *our greatest opportunity for future growth lies in our silicon division, particularly the solar-grade silicon component of the business. We believe that this is a great time to be in business of silicon.*

* * *

Our historical silicon business with more than three decades of experience is already a North American leader in the manufacture of silicon metal and ferrosilicon products. We have an annual production capacity of 50,000 metric tons. We supply to four of the world's major silicon and polysilicon manufacturers.

We believe that strong results in our historical silicon business will be driven by favorable market conditions, in particular the rising price for silicon. But even more promising than price recovery is *our entry into the production of solar-grade silicon, which will provide tremendous upside.* We will transition increasing portions of our output from our historical silicon business to supply our solar-grade silicon operations.

* * *

The solar energy industry is still in its relative infancy, so there are no entrenched suppliers of solar-grade silicon. *We believe we are well positioned to capitalize on this largely untapped market. We aim to establish ourself as the leading global supplier of low-cost solar-grade silicon to the manufacturers of solar cells.*

Our proprietary metallurgical base process for the production of solar-grade silicon provides us with a significant cost advantage, based on required capital expenditures, electricity -- the single largest input cost in the production of solar-grade silicon -- and raw materials.

Our process, which has two patents pending, requires capital investment that is significantly lower than conventional polysilicon processes and electricity costs that can be as little as 1% of polysilicon [processing].

* * *

> Our growth strategy for our solar silicon business is focused on two key areas -- developing long-term relationships with manufacturers of solar wafers and cells; and building our production capacity to meet existing and anticipated customer demand.

[Emphasis added].

32. These statements represented, falsely, that Timminco was "well positioned" as a low-cost producer of solar-grade silicon and had "a significant cost advantage" that was "a tremendous upside" for the Company. Accordingly, the representations made in the March 2008 Conference Call were Misrepresentations.

33. Following the March 2008 Press Release and the March 2008 Conference Call, the price of Timminco shares on the TSX increased from $17.29 on March 17, 2008 to $27.49 on March 27, 2008.

2007 Annual Information Form

34. On March 28, 2008, Timminco published its 2007 Annual Information Form on SEDAR. The 2007 Annual Information Form is a Core Document.

35. The 2007 Annual Information Form states:

> Overview
>
> The Company is a leader in the production and marketing of lightweight metals, specializing in solar grade silicon for the solar photovoltaic ("PV") energy industry.
>
> * * *
>
> *The Company has expanded its solar grade silicon production capacity to 3,600 metric tons per year, and plans to further increase capacity to meet current and anticipated demand.*
>
> * * *
>
> Silicon Business
> Solar Grade Silicon

The Company uses a patent-pending process to purify low purity metallurgical grade silicon into higher purity solar grade silicon (also known as upgraded metallurgical silicon) for manufacturers of solar wafers and solar cells... *The Company's proprietary process requires significantly less capital investment and uses considerably less electricity than for the production of polysilicon.*

* * *

The Company built a small scale production facility in late 2006 to test its proprietary purification process. Based on the initial success of this process, and the execution of initial long-term contracts with customers for the supply of the Company's solar grade silicon in early 2007, the Company commenced construction of a 3,600 metric ton production facility for solar grade silicon in August 2007, which facility was completed in February 2008. By the end of 2007, the Company had entered into four long-term contracts for the supply of solar grade silicon through 2012, and had received orders from customers, which accounted for all of the Company's planned production capacity in 2008. In February 2008, the Company announced plans to quadruple its production capacity of solar grade silicon from 3,600 to 14,400 metric tons by mid-2009, to meet customer commitments under long-term contracts and to satisfy anticipated further demand. In March 2008, the Company executed a fifth contract with the world's largest solar cell manufacturer, to supply solar grade silicon in 2008 and 2009, with a possibility to extend the term from 2010 to 2013 with increased volumes.

* * *

The Company produces solar grade silicon using a proprietary manufacturing process to purify low purity metallurgical grade silicon, which yields upgraded metallurgical silicon with a purity level of 99.999% or "5-nines", and an impurity count of 0.8 parts per million (ppm) of boron and less than 5.0 ppm of phosphorous. At these levels, the Company's solar grade silicon can be successfully used in the production of solar cells.

* * *

The Company manufactures solar grade silicon by purifying silicon metal. The purification process begins with molten silicon metal and consists of multiple steps to yield solar grade silicon with the desired purity level (99.999%, or "5-nines", pure) and impurity counts for phosphorous and boron. The equipment and methods used by the Company to purify silicon metal in its solar grade silicon production are based on two patents pending manufacturing processes. In particular, during 2007 the Company filed a formal patent application with the U.S. and international patent authorities in respect of one of its processes for purifying low-grade silicon metal. The Company has a 2006 priority date in respect of this patent application, and the international patent examiner has provided a positive report on such application. The Company has also filed a formal patent application in 2008 with the U.S. and international patent authorities in respect of another process for purifying low-grade silicon metal, which claims a 2007 priority date...*These patents are fundamental to the Company's purification processes and a key component in the competitive advantage of the Company's solar grade silicon business.* The Company has also filed other informal (or provisional) patent applications relating to solar grade silicon production.

* * *

The following are competitive strengths of the Company's solar grade silicon business:

Proprietary Process for Purifying Metallurgical Grade Silicon. The Company's proprietary technology for purifying metallurgical grade silicon into high purity silicon metal is a significant competitive advantage of the Company. The most important specifications of solar grade silicon for manufacturers of solar cells is purity, in particular boron and phosphorous levels. The Company has been able to produce high purity silicon with 0.8 ppm boron and less than 5.0 ppm phosphorous using [sic]...

Cost Advantages Relative to Polysilicon. The Company's proprietary process offers significant cost advantages based on efficiencies in three main areas: capital expenditures, raw materials and electricity used in the solar grade silicon production process. The capital investment required for the production of solar grade silicon is not insignificant. Conventional polysilicon processes can require capital investments of as much $100 per kilogram of annual capacity (which equates to a $500 million investment for 5,000 metric tons of output), and even more for new entrants to the market, whereas the capital investment for the Company's process is up to 20 times lower (the Company invested $24 million to build 3,600 metric tons of annual capacity). The cost of electricity used in the Company's process is as little as 2% of that used in conventional polysilicon processes, which require up to 135 kilowatt hours per kilogram of output, compared to 2 kilowatt hours per kilogram of output required by the Company's process. Finally, the Company's process allows the use of less expensive raw materials to produce solar grade silicon that meets our customers' specifications. The Company believes that it can achieve an average cost of $12 per kilogram for 2008, approximately half that of the $2 to $25 per kilogram that it generally costs existing polysilicon producers.

Ability to Rapidly Increase Production Capacity. The Company also has a significant advantage in the time it takes to add production capacity for solar grade silicon. The Company can significantly expand capacity in less than one year, whereas polysilicon producers, in contrast, typically require at least three to four years to do the same. Moreover, despite the current shortage of supply in the marketplace, existing market participants are generally resistant to adding capacity due to both the significant investment and the long time horizon.

* * *

The Company's new solar grade silicon production facility in Becancour, having a production capacity of 3,600 metric tons per year, only started production on the third of its three 1,200 metric ton production lines in February 2008. *The Company has experienced and expects to continue to experience rapid growth rates in this business and the solar photovoltaic energy industry generally.*

* * *

The Company is currently able to produce solar grade silicon at a purity level of 99.999% or "five nines", with levels of phosphorous and boron that are acceptable to existing customers.

36. The 2007 Annual Information Form represented, falsely, that Timminco "is a leader in the production and marketing of lightweight metals, specializing in solar grade silicon for the solar photovoltaic ("PV") energy industry", and that it had "expanded its solar grade silicon production capacity to 3,600 metric tons per year". Furthermore, the 2007 Annual Information Form represented, falsely, that Timminco's "proprietary process requires significantly less capital investment and uses considerably less electricity than for the production of polysilicon", and that Timminco's solar grade silicon can be successfully used in the production of solar cells[2], with "levels of phosphorous and boron that are acceptable to existing customers."

37. The 2007 Annual Information Form also represented that Timminco's "proprietary technology for purifying metallurgical grade silicon into high purity silicon metal is a significant competitive advantage of the Company", that "[t]he Company's proprietary process offers significant cost advantages based on efficiencies in three main areas: capital expenditures, raw materials and electricity used in the solar grade silicon production process", and that "[t]he Company also has a significant advantage in the time it takes to add production capacity for solar grade silicon."

38. The above statements omitted to state that Timminco's solar-grade silicon production process was not capable of producing silicon at the quantity, cost and impurity composition that would be commercially viable. While the impurity concentrations may have been acceptable to its existing customers, Timminco failed to disclose that this impurity composition was not

generally commercially acceptable and that it could not produce solar-grade silicon at a generally commercially acceptable impurity composition in commercial quantity. This inability would have a detrimental effect on the Company's revenues and profits. Accordingly, the representations made in the 2007 Annual Information Form were Misrepresentations.

2007 MD&A

39. On March 28, 2008, Timminco published its 2007 MD&A on SEDAR. The 2007 MD&A is a Core Document. The 2007 MD&A stated:

> Construction of the new 3,600 metric ton solar grade silicon manufacturing facility was completed on schedule with commissioning of the three 1,200 metric ton lines completed in February 2008.
>
> * * *
>
> The Company has constructed a new manufacturing facility at its Bécancour location having an annual capacity to produce 3,600 metric tons of solar grade silicon...The Company commenced construction of this new facility in August 2007, which consists of three separate production lines, each expected to yield at least 1,200 metric tons of annual capacity, for a total capacity of 3,600 metric tons per year. The first of the three lines was commissioned in December 2007 and the second and third lines came on stream in February 2008. *It is anticipated that full production capacity of these three production lines will be reached in the beginning of the third quarter 2008.*
>
> On February 22, 2008, *the Company announced plans to further expand its solar grade silicon production capacity, from 3,600 metric tons to 14,400 metric tons per year.*
>
> * * *
>
> The success of the Company's solar grade silicon business depends to a large degree on the protection of its intellectual property rights, including proprietary technology, information, processes and know-how. Such protection is based on trade secrets and patents, including two patents pending in respect of the Company's manufacturing process for the production of solar grade silicon.
>
> * * *
>
> The Company's growth strategy is straight forward: *Leverage its competitive advantages in the production of solar grade silicon to establish long-term relationships with major players in solar cell manufacturing, and continue to*

> *expand its capacity to meet this demand. With a significant shortage in today's solar grade silicon market, the Company's ability to offer an alternative source of supply provides an opportunity to capture market share.* During 2008, the Company expects to enter into additional long-term contracts for solar grade silicon that will be produced in its expanded solar grade silicon facilities in 2009.

40. The 2007 MD&A represented, falsely, that Timminco could "[l]everage its competitive advantages in the production of solar grade silicon". In addition, the Company characterized its process as unique and proprietary technology, when in fact the process utilized refurbished common industrial equipment. Timminco's solar-grade silicon production process was not capable of producing at commercially acceptable impurity composition, or at the quantity, cost and impurity composition consistent with the statements contained in the MD&A. The statements contained in the 2007 MD&A were Misrepresentations.

Certification of Filings

41. Schimmelbusch and Dietrich each certified that the 2007 MD&A, to their knowledge, did not contain any untrue statement of a material fact or omit to state a material fact required to be stated or that is necessary to make a statement not misleading in light of the circumstances under which it was made.

42. At the time of the said certifications, Schimmelbusch and Dietrich knew or ought to have known or were reckless in not knowing, that the 2007 Annual Report, the 2008 First Quarter Results and the MD&A Q1 2008 contained untrue statements of material fact and further or in the alternative, omitted to state a material fact required to be stated or that was necessary to make a statement not misleading in light of the circumstances in which it was made, as set out above.

The 2007 Annual Report

43. On March 31, 2008, after the close of trading on the TSX, Timminco published its 2007 Annual Report on SEDAR. The 2007 Annual Report is a document that would reasonably be expected to affect the market price of the shares in Timminco.

44. The 2007 Annual Report states:

> We are a leader in the production and marketing of lightweight metals, specializing in solar-grade silicon for the rapidly growing solar photovoltaic energy industry. We produce approximately 50,000 metric tons of silicon metal per year, from which *we use our proprietary technology to produce low-cost solar-grade silicon for use in the manufacture of solar cells and modules. We have expanded our solar-grade silicon capacity to 3,600 metric tons per year, and plan to further increase capacity to 14,400 metric tons per year to meet anticipated demand.* We produce silicon metal, magnesium extrusions and other specialty metals for use in a broad range of industrial applications serving the aluminum, chemical, pharmaceutical, electronics and automotive industries. *With proven expertise in the silicon industry, proprietary technology and the ability to rapidly scale up production capacity, we are well-positioned to establish ourselves as a leading supplier of low-cost solar-grade silicon.*
>
> * * *
>
> Silicon Metal Business
>
> With more than 30 years of experience, we are one of North America's largest producers of silicon metal, as well as other forms of silicon, including ferrosilicon. Our 60-acre facility in Bécancour, Québec has an annual production capacity of 50,000 metric tons (mt) per year. Our products are used primarily in the chemical, electronics, aluminum, iron and steel industries, as well as for the production of polysilicon by suppliers to the manufacturers of solar cells for the solar photovoltaic (PV) energy industry. *Our proprietary compound electrode processes provide us with a significant cost advantage in the industry.*
>
> Solar-grade Silicon Business
>
> We are leveraging our experience and expertise in the production of metallurgical silicon to produce and market solar-grade silicon for the high growth solar photovoltaic (PV) energy industry. *Our proprietary technology enables us to process metallurgical grade silicon into higher purity solar-grade silicon (using a metallurgical process) for use in the manufacture of solar cells. The solar-grade purity level of our product provides an additional source of supply to manufacturers in today's supply-constrained market. Because our process requires significantly lower capital investment and uses considerably less*

electricity than conventional silicon purification processes, our solar-grade silicon is a low cost alternative to the industry's mainstay, polysilicon. Our historical silicon metal business ensures that we will have the feedstock to support the expansion of our capacity to build long-term customer relationships.

* * *

As the solar PV energy industry realizes its projected growth, *we are well positioned to become a leading supplier of solar-grade silicon to the manufacturers of solar cells. Our proprietary technology for processing low-purity, metallurgical grade silicon into higher purity solar-grade silicon provides us with a considerable competitive advantage in the marketplace. Significantly lower capital costs and requirements for electricity, the largest input cost in the production of solar-grade silicon, compared to our competitors, positions us as a low-cost producer. In fact, the cost per kilogram of our process can be as much as half that of conventional processes.* Furthermore, we have the advantage of security of supply of feedstock through our upstream integration.

* * *

The most important specification of solar-grade silicon for manufacturers of solar cells is purity, in particular boron and phosphorous levels. We are continually refining our production process to improve the purity of our product, which will not only expand our base of potential customers, but will also command higher prices in the market. Earlier this year, we achieved a significant milestone in this pursuit when we started to produce silicon with 0.8 parts per million (ppm) boron and less than 5.0 ppm phosphorous. We are confident that we can continue to improve upon this mark.

* * *

Increasing the Purity of Solar-grade Silicon

The Company is currently able to produce solar-grade silicon at a purity level of 99.999%, or "five nines", with levels of phosphorus and boron that are acceptable to existing customers. Achieving a higher purity level could enhance the Company's competitive advantage and may allow for increased selling prices and margins for the solar-grade silicon business. The Company intends to invest certain resources in an effort to achieve an improvement in, and maintain the consistency of, purity levels of its solar-grade silicon. However, there is no assurance that the Company will consistently achieve any higher purity level for its solar grade silicon.

* * *

We have developed a proprietary metallurgical-based process for the production of solar-grade silicon that has a number of important advantages over conventional chemical-based processes. Our process, which has two patents pending, begins with molten silicon and consists of multiple steps to yield solar-grade silicon with a purity of 99.999% and an impurity count of 0.8 parts per

168

> *million (ppm) of boron and less than 5.0 ppm of phosphorous, which can be successfully used in the production of solar cells. Through continual refining of our process, we expect to further improve upon these levels.*
>
> *Our process offers significant cost advantages based on efficiencies in three main areas: capital expenditures, raw materials and electricity used in the production process.* The capital investment required for the production of solar-grade silicon is not insignificant. Conventional polysilicon processes can require capital investments of as much as $100 per kilogram (a $500 million investment for 5,000 mt of annual output), and even more for new entrants to the market. *The capital investment for our process is up to 20 times lower* – last year we invested just $21.7 million to build 3,600 mt of capacity.
>
> * * *
>
> The manufacture of solar cells requires silicon that is at least 99.999% (5-nines) pure. *Our proprietary metallurgical process enables us to achieve these levels with significantly lower capital investment and production costs than conventional chemical processes used for the semiconductor industry.*

[Emphasis added].

45. The statements in the 2007 Annual Report represented that:

(a) Timminco had a "competitive advantage" because its "proprietary process" enabled it "to process metallurgical grade silicon into higher purity solar-grade silicon" with "a significant cost advantage";

(b) Timminco's "proprietary technology and the ability to rapidly scale up production capacity" rendered the Company "well-positioned to establish [itself] as a leading supplier of low cost solar-grade silicon."; and,

(c) Timminco's process was state of the art and a unique technology.

46. Each of the said representations was false or misleading. In fact, Timminco was unable to produce solar-grade silicon at a commercially acceptable impurity composition, and its process utilized refurbished common industrial equipment, and so its processes could not be considered "state of the art" or unique technologies. Further, while the impurity composition of Timminco's solar-grade silicon production may have been acceptable to its existing customers, Timminco failed to disclose that this impurity composition was not generally commercially acceptable and that Timminco could not produce solar-grade silicon at a generally commercially

acceptable impurity composition in commercial quantity, and accordingly the 2007 Annual Report contained Misrepresentations.

47. Following the issuance of the 2007 Annual Report, the price of Timminco shares on the TSX increased from $23.26 on April 1, 2008 to $28.00 on April 10, 2008.

Media Criticism of Timminco

48. In April 2008, negative media reports emerged questioning whether the Company's claims relating to its low-cost production of silicon were valid.

49. On April 21, 2008, Barron's Bill Alpert published an article entitled, "Timminco Generates More Heat Than Light - Are Timminco's claims of a low-cost way to purify silicon too good to be true?" According to the article, "[t]he justification for Timminco's share appreciation is supposed to be its invention of a low-cost way to purify the silicon needed for the booming solar-cell market. But so far, the evidence for Timminco's breakthrough appears in PowerPoint slides, not financial reports."

50. On April 23, 2008, Bloomberg published an article entitled, "Timminco Falls on Concern New Technology Won't Satisfy Clients," criticizing the Company's failure to respond to investor concerns that the Company's much publicized low-cost method of purifying silicon could possibly not meet customer demands. The article stated:

> The company hasn't dispelled claims in publications including Barron's and the Globe and Mail that the technology Timminco is using to supply the world's biggest solar-cell manufacturer may not meet specifications, said John Stephenson, who helps oversee about $1.62 billion as a portfolio manager at First Asset Investment Management Inc. in Toronto.
>
> "The best one can say is that Timminco's management has handled this poorly," Stephenson said. "It's a headscratcher. How does a company spending about C$2 million on R&D come up with something that Dow Corning can't do?"

51. Also on April 23, 2008, Timminco issued a press release which stated that it was unaware of any corporate developments that would explain recent trading activity in Timminco's stock. On the same day, *Reuters* published an article entitled, "Update 2 - Timminco says can't explain volatility, stock up" addressing the Company's attempts at the request of TSX's Market Surveillance wing to "fend off aggressive short selling and assuage growing concerns over whether it will be able to satisfy customers in the burgeoning solar-cell industry." The article also reported that infamous short seller Manuel Asensio had "challenged Timminco's assertions that it can purify metallurgical grade silicon in a cost-efficient way for use in solar power cells." ~~Timminco issued the statement that it had no explanation for the volatility of the Company's stock.~~

The Photon Report

52. In response to this media criticism, Timminco and the Individual Timminco Defendants retained, or authorized, permitted or acquiesced in the retention of, Photon Consulting, Rogol Energy, solar-power consulting and research firms, and Michael Rogol, to examine and evaluate the business. Their report (the "Photon Report") was issued on or about May 8, 2008.

53. On May 8, 2008, Timminco issued a press release ~~announced~~ announcing that it had received the Photon Report concerning its silicon production process and plant. The Photon Report was subsequently posted on Timminco's website on May 14, 2008. In the Report, Photon Consulting states that it "serves the solar and silicon sector by providing accurate information and analysis," and states that it has an "experienced, multi-disciplinary team". The Photon Report is a document that would reasonably be expected to affect the market price of the shares in Timminco.

54. The Photon Report was based on a one-day facility visit to the Bécancour facility by a Photon Consulting team in early May, 2008. In the May 8, 2008 press release Timminco stated that the Photon Consulting team was given full access to the solar grade silicon production facility and to information relating to accounting procedures, R&D efforts, human resource needs, intellectual property, and technical process that were requested to prepare the report.

55. The Photon Report indicated that the "[o]perations and processes have potential for massive growth and, possibly, for reshaping [the] industry", and that the "[e]quipment [was] very impressive, very low cost, 'beyond poly' scale...." The Photon Report also projected the "potential for ~$270mn to ~$1bn in operating profit by 2010", and a operating margin of "50% to 80% in 2010".

56. The Photon Report contained the following positive statements regarding Timminco's operations in its review report:

(a) "Timminco's material works now and will work even better with practice";

(b) "Impressive operations today with significant improvement potential and manageable constraints"; and,

(c) "Transparency on accounting signals honest reporting. Accuracy will improve with scale & consistency of operations".

57. The Photon Report omitted to state that Timminco's solar-grade silicon production process was not capable of producing silicon at commercially acceptable impurity composition, or at the quantity, cost and impurity composition consistent with the statements contained in the Photon Report. The Photon Report therefore contained Misrepresentations.

2008 First Quarter Results

58. On May 8, 2008, Timminco also announced its financial results for the first quarter ended March 31, 2008 by way of a separate press release. ~~The~~ This ~~P~~press ~~R~~release is a document that would reasonably be expected to affect the market price of the shares in Timminco. .

59. The May 8, 2008 ~~P~~press ~~R~~release stated that:

(a) Timminco completed the commissioning of a solar-grade silicon production facility with nominal annual production output of 3,600 metric tons;

(b) Timminco shipped 100 metric tons of solar-grade silicon at an average selling price in excess of $60 per kilogram;

(c) cash and short-term investments as at March 31, 2008 were $11.3 million compared to $34.6 million at the end of 2007. During the quarter, $6.2 million was invested in working capital to support the 31% increase in sales volumes over the fourth quarter of 2007, $16.5 million was spent on capital expenditures relating primarily to the solar grade silicon facilities and $1.9 million was invested in Fundo Wheels to support the turnaround of that business; and,

(d) sales of the Silicon Group were $34.7 million in the first quarter of 2008, an increase of 45.2% from $23.9 million of first quarter of 2007. The increase in sales was due to the growth in sales of solar grade silicon and an increase in sales volume of regular grade silicon metal.

The May 8, 2008 Conference Call

60. On May 8, 2008, Schimmelbusch and Boisvert conducted the May 8, 2008 Conference Call with analysts and investors. Throughout the May 8, 2008 Conference Call, Schimmelbusch and Boisvert made Public Oral Statements relating to the business, operations, and affairs of Timminco.

61. During the May 8, 2008 Conference Call, Schimmelbusch stated:

> *I believe we are uniquely positioned to become the leading provider of low-cost solar-grade silicon, and capitalize on a market where demand is high and is expected to grow. I believe we will realize our potential through our state-of-the-*

art production facilities, patent-pending processes, and pedigree in the silicon metal business.

62. In response to a question relating to Timminco's competitive positioning and advantages relative to the other existing metallurgical companies and the other purification techniques disclosed by Timminco's competitors, Schimmelbusch stated:

> We know that there are two or three serious attempts in this area and more -- and maybe more which are not yet published. *We believe that we have a very competitive process and a very competitive product. And we believe that our CapEx per unit of capacity is especially competitive given the efficiency of our process and the -- if you allow me, the elegance of this technological concept. . . . But our competitiveness is certainly established at the unit cost level, in my estimation, in my opinion. And it is particularly established in the CapEx per capacity unit. And that is very important for the scalability of such an operation. We believe that we can model an add-on capacity in a very efficient way with very low -- or the relatively low additional CapEx needs. And that will ultimately be a big competitive instrument.*

[Emphasis added]

63. Schimmelbusch explained that he had commissioned the Photon Report in order to address media criticism questioning the Company's claims relating to its process, noting that the Company's process had never been independently verified, and observing that rival companies had spent far more trying to upgrade metallurgical silicon to solar-grade level with less success. Schimmelbusch further stated:

> We have been criticized consistently that we haven't invited, that we didn't have an open house policy and invite everybody to walk through the plants.
>
> I have been in the industry for a very long time, in the metal industry, in all aspects of it. It is so that a process technology, especially a process technology of this kind, is a key competitive instrument. The idea to show to an engineering firm, or to experienced engineers which might talk to the competition, if you have a breakthrough innovation like this, is detrimental to shareholder value.
>
> The -- we had advice -- or unasked for advice by the media to do that. So, the media were advising us to follow a strategy which will actually destroy shareholder value, inviting imitation of our -- the technology, competitive advantage in other plants and other companies. So, we have resisted that.

> We felt that the integrity and the reputation which they want to keep of Photon would shield us against any outflow of competitive important information while, at the same time, giving us -- giving a comfortable statement here. So, that was the fine line which we had to follow in making that decision.

64. During the May 8, 2008 Conference Call, Boisvert stated that the Company had provided open access to the Photon Consulting team:

> The due diligence performed by Photon Consulting was done by a team of people that were given access to all of our production facility. They reviewed the process. They reviewed the accounting in detail. They met with all the different management people on one-to-one sessions, interviewing them to the point where some people even felt uneasy about the amount of information that was transferred. So, we were completely transparent and open, answered all of their questions, and just received their report this morning.

65. The Public Oral Statements made by Schimmelbusch and Boisvert in the May 8, 2008 Conference Call represented, falsely, that Timminco was competitive as a low-cost silicon provider and that Timminco "will realize [its] potential through [its] state-of-the-art production facilities", and misleadingly implied that it was capable of producing solar-grade silicon with commercially acceptable impurity composition, and of producing same at the quantity and cost as set out in the May 8, 2008 Conference Call, and, accordingly, the representations made during the May 8, 2008 Conference Call were Misrepresentations.

66. Timminco's financial statements, including the 2007 Annual Report and the 2008 First Quarter Results, were approved by the company's board of directors before the statements were filed, pursuant to the requirements of s. 4.5 of National Instrument 51-102.

67. On May 8, 2008, following the public release of the First Quarter Results, the Photon Report, and the May 8, 2008 Conference Call, the price of Timminco shares on the TSX increased from $23.70 to $24.60.

MD&A Q1 2008

68. On May 13, 2008, Timminco published its MD&A discussing financial results for fiscal year 2007 and first quarter 2008 on SEDAR. The MD&A is a Core Document.

69. The MD&A stated:

> *The first quarter of 2008 saw continued progress towards the Company's goal of increasing solar-grade silicon production and sales and continuing towards the further expansion of the Company's solar-grade silicon manufacturing facility.*
>
> Sales for the first quarter were $47.6 million compared with $42.8 million in the first quarter of 2007, an increase of 11.2%. The increase is attributable to growth in the sales of the Company's solar grade silicon and silicon metal products. For the first quarter, the net loss was $0.6 million or ($0.01) per share, compared with a loss of $3.1 million in the first quarter of 2007 ($0.04) per share.
>
> * * *
>
> On February 22, 2008, the Company announced its plans to expand capacity for the production of solar-grade silicon at its wholly owned subsidiary, Bécancour Silicon Inc. ("BSI"), at its location in Bécancour, Québec. *The expansion is expected to raise the total annual production capacity of its solar-grade silicon facilities to 14,400 metric tons from 3,600 metric tons.* The expansion is expected to have a capital cost of approximately $65 million and will be completed by mid 2009, on a schedule that will enable BSI to meet all current customer commitments.
>
> * * *
>
> *Increasing the Purity of Solar Grade Silicon*
>
> The Company is currently able to produce solar grade silicon at a purity level of 99.999%, or "five nines", with levels of phosphorus and boron that are acceptable to existing customers. The Company has targeted to improve the boron impurity level from 0.8 parts per million to 0.5 parts per million and the phosphorous impurity level from 3.0 parts per million to 1.5 parts per million by the end of the year. Achieving a higher purity level could allow customers to increasingly utilize unblended versions of the Company's solar grade silicon in their manufacturing activities, which could enhance the Company's competitive advantage and may allow for increased selling prices and margins. The Company intends to invest certain resources to achieve these improvements in purity levels of its solar grade silicon. However, there is no assurance that the Company will consistently achieve any higher purity level for its solar grade silicon.

[Emphasis added]

70. The MD&A Q1 2008 misrepresented that Timminco had made "progress towards the Company's goal of increasing solar-grade silicon production" and that "[t]he expansion is expected to raise the total annual production capacity of its solar-grade silicon facilities to 14,400 metric tons from 3,600 metric tons." Timminco falsely implied that it was capable of producing solar-grade silicon with commercially acceptable impurity composition, and of producing same at the quantity and cost as set out in the MD&A Q1 2008, and, accordingly, the representations made in the MD&A Q1 2008 were Misrepresentations.

Certification of Filings

71. Schimmelbusch and Dietrich each certified that the 2007 Annual Report, the 2008 First Quarter Results and the MD&A Q1 2008, to their knowledge, did not contain any untrue statement of a material fact or omit to state a material fact required to be stated or that is necessary to make a statement not misleading in light of the circumstances under which it was made.

72. At the time of the said certifications, Schimmelbusch and Dietrich knew or ought to have known or were reckless in not knowing, that the 2007 Annual Report, the 2008 First Quarter Results and the MD&A Q1 2008 contained untrue statements of material fact and further or in the alternative, omitted to state a material fact required to be stated or that was necessary to make a statement not misleading in light of the circumstances in which it was made, as set out above.

The May ~~13~~14, 2008 Conference Call

73. On May ~~13~~14, 2008, Schimmelbusch and Michael Rogol conducted the May ~~13~~14, 2008 Conference Call with analysts and investors. Rogol had the actual, implied or apparent authority to speak on behalf of Timminco by virtue of the Company's issuance of the Photon Report and

its inclusion of Rogol on the conference call to speak for the Company. Rogol was the expert hired by Timminco through Photon Consulting and Rogol Energy. Rogol was the Managing Director of Photon Consulting. Throughout the May ~~13~~14, 2008 Conference Call, Schimmelbusch and Rogol made Public Oral Statements relating to the business, operations, and affairs of Timminco. Schimmelbusch and Rogol quoted from and summarized the Photon Report.

74. During the May ~~13~~14, 2008 Conference Call, Rogol described the preparation of the Photon Report and Timminco's silicon production process. He downplayed analyst questions relating to the quality and purity of the solar-grade silicon being produced by Timminco.

75. Rogol stated that Photon Consulting had interviewed customers who were satisfied with the product and unconcerned with boron and phosphorous impurity levels because "it works." While declining to make any "robust statements" without further data, Rogol explained that if customers were concerned with the purity level of the solar-grade silicon they would be requesting significant discounts, and he reported that was not the case, thereby plainly implying that phosphorous contamination was not an issue for Timminco.

76. A slide presentation accompanied the May ~~13~~14, 2008 Conference Call. The slide presentation summarized and quoted from the Photon Report and stated in relevant part:

(a) Impressive operations, Equipment: Very Impressive, very low cost, beyond "poly" scale;

(b) 2010 UMG-Si outlook, production volume, 12,000 to 20,000 ton/year in 2010;

(c) Revenue: $540 million to $1.3 billion in 2010;

(d) Operational profit: $270mn to ~ $1 billion in operating profit in 2010*;

(e) Operational margin: 50% - 80% in 2010*;

(f). Potential for ~ $270mn to ~ $1bn in operating profit by 2010.

77. The representations made by Schimmelbusch and by Rogol as an expert and on behalf of the Company (including the slide presentation) made during the May ~~13~~14, 2008 Conference Call represented, falsely that Timminco's silicon production process "works." ~~Regel~~Rogol, on behalf of the Company, omitted to state that Timminco's solar-grade silicon process was not capable of producing solar-grade silicon with commercially acceptable impurity composition, and of producing same at the quantity and cost as stated by him, and accordingly, the representations made in the May ~~13~~14, 2008 Conference Call were Misrepresentations.

78. Following the MD&A and the May ~~13~~14, 2008 Conference Call, the price of Timminco shares on the TSX increased from $23.27 on May 13, 2008 to $28.95 on May 16, 2008.

The May 29, 2008 Conference Call

79. On May 29, 2008, Schimmelbusch conducted the May 29 Conference Call with analysts and investors. Throughout the May 29 Conference Call, Schimmelbusch made Public Oral Statements relating to the business, operations, and affairs of Timminco.

80. During the May 29, 2008 Conference Call, Schimmelbusch stated:

> Our Bécancour facility has a number of strategic advantages. It has ready access to hydroelectricity, needed for our production of silicon metal, is core located with our silicon metal business for process efficiency, has a 30-year history with an experienced staff, and has easy access to transportation routes. *Our competitive advantage is clear. We have a patent-pending process, we employ low cost production technologies, as evidenced by our capital investments in a new facility, lower energy costs, and less costs for raw materials, we have the ability to add capacity, we have constant access to raw materials, and ready access to electricity. Combined, these make Timminco a force to be reckoned with in the solar energy industry.*
>
> We are receiving validation and positive feedback from the industry. We have six long-term contracts in place to supply more than 9,000 metric tons annual beginning in 2009. In 2010, this number will grow to 15,000 metric tons. In the

> first quarter, we signed a major long-term agreement with Q-Cells, the world's largest manufacturing of -- manufacturer of solar cells to supply more than 3,400 metric tons of solar-grade silicon by the end of 2009, with the potential of increasing that total to 6,000 metric tons per year beginning 2010. We received an extremely positive endorsement of our manufacturing process and production capabilities from Photon Consulting, the leading analysts for the solar energy industry. Some of our customers are using Timminco material 100% unblended with other elements. This results in reduced costs for our customers, and strengthens our position in terms of their supply chain.

[Emphasis added].

81. Schimmelbusch also placed emphasis on the Company's proprietary purification process, stating: ". . . it is important to note that the Company's technology is also protected by the fact that one key element, one key equipment, which is necessary to operate our purification process is very proprietary equipment where we have exclusive use, which is sort of a second level of protection beyond patent." He also touted the Company's "state-of-the-art facilities" as a reason for its "considerable progress towards our vision of becoming a leading low-cost provider of solar-grade silicon."

82. The Public Oral Statements made during the May 29, 2008 Conference Call represented, falsely, that Timminco was a low-cost producer of solar-grade silicon, and further misleadingly implied that it was capable of producing solar-grade silicon with commercially acceptable impurity composition, and of producing same at the quantity and cost as set out in the May 29, 2008 Conference Call, and accordingly, these representation were Misrepresentations.

83. Following the May 29, 2008 Conference call the price of Timminco shares on the TSX increased from $28.00 to $35.69 on June 5, 2008.

84. The statements contained in each of the March 2008 Press Release, the March 2008 Conference Call, the 2007 Annual Information Form, the 2007 MD&A, the 2007 Annual Report, the Photon Report, the 2008 First Quarter Results, the May 8, 2008 Press Release, the May 8,

2008 Conference Call, the MD&A Q1 2008, the May ~~13~~14, 2008 Conference Call, and the May 29, 2008 Conference Call omitted to state that Timminco's solar-grade silicon production process was not capable of producing silicon at quantity, cost, and purity levels consistent with Company statements, and that this inability would have a detrimental effect on the Company's revenues and profits. Instead, Timminco retained its existing revenue and production forecasts. Each of these written representations and Public Oral Statements were Misrepresentations.

THE TRUTH BEGINS TO EMERGE

85. On August 11, 2008, after the TSX closed, Timminco issued the August 11, 2008 News Release, announcing its financial results for the second quarter ended June 30, 2008, and conducted a follow-up August 11, 2008 conference call with investors and analysts. In the conference call, Schimmelbusch and Boisvert conceded that Timminco's solar-grade silicon production process had experienced contamination problems resulting from the use of equipment that was not intended for use in the manufacture of silicon and that these contamination problems in turn impaired the Company's financial performance. In response to questions from Michael Willemse, an analyst with CIBC World Markets, Schimmelbusch and Boisvert for the first time disclosed that Timminco's technology was not perfected, its silicon production equipment was designed for "different purposes, namely for ... the aluminum industry,", that the use of such equipment had caused phosphorus contamination problems in the silicon production process, and that the Company had to undertake "debugging" operations, which the Company knew would be required.

86. Timminco's share price dropped from $19.97 on August 11, 2008 to $12.25 on August 14, 2008, as a result of the disclosure that the Company's proprietary process used to produce low-cost solar-grade silicon was flawed.

87. The August 11, 2008 News Release and the August 11, 2008 Conference Call did not fully correct the Misrepresentations made by Timminco in its previous public and financial disclosure as set out above. Among other things, Timminco maintained the Photon Report posted on its website, including its "extremely positive endorsement" of the Company and its manufacturing process and production capabilities, and the Company did not revise its previously released production and revenue forecasts.

88. On November 11, 2008, after the TSX closed, Timminco announced that it was removing the Photon Report and related documents (which had been posted on May 14 and August 12, 2008) from its website on the ground that "some of the material factors or assumptions originally used to develop the forward-looking information in the Photon Report, including in respect of revenues, production line volumes and costs, may no longer be valid."

89. The Company's share price dropped from $7.93 on November 11, to $6.71 on November 12, and further to $3.37 on November 19, 2008.

90. On November 15, 2008, the *Financial Post* published an article on Timminco which referenced concern about Timminco's disclosure record, and stated that the Company was removing the positive Photon Report from its website, which "the company said it 'originally commissioned ... to support due-diligence efforts for strategic discussions beyond normal supplier-customer relationships and made it publicly available to enhance the investing public's understanding of the potential future performance for Timminco's solar-grade silicon product line.'". The Photon Report was removed from the website on the basis that "Timminco (now) 'believes that some of the material factors or assumptions originally used to develop the forward-looking information in the Photon Report, including in respect of revenues, production volumes and costs, may no longer be valid'".

SUBSEQUENT EVENTS

91. Since the corrective statements were made, Timminco's share price has continued to drop. In April 2009 Timminco announced that certain of its solar-grade silicon customers had terminated their contracts for non-compliance. In May 2009 Timminco released its first quarter results for 2009. On May 12, 2009, the share price had dropped to $1.84 per share.

THE RELATIONSHIP BETWEEN THE MISREPRESENTATIONS AND THE PRICE OF TIMMINCO'S SECURITIES

92. Timminco's securities were and are publicly traded on the TSX, which is a highly efficient and automated market. Any and all public information regarding Timminco is promptly incorporated into, and has as direct effect upon, the price of Timminco's shares. As such, the price of Timminco's publicly-traded securities was directly affected by the press releases, conference calls, quarterly reports, annual reports, MD&A, and the Photon Report described herein.

93. The disclosure documents and statements referenced above, and all the information contained therein, including the Misrepresentations, were immediately made available to the Plaintiff, other Class Members, other members of the investing public, financial analysts, and the financial press. The Defendants were aware of this fact at all material times, as evidenced by the following:

(a) the disclosure documents were filed with SEDAR and the TSX and were immediately accessible by the public;

(b) copies of the disclosure documents, or links to them, were provided by Timminco on its website; and,

(c) the Defendants regularly communicated with the investing public and financial analysts through press releases on newswire services and other established market communication mechanisms.

94. Any and all analysis undertaken by the Plaintiff and other Class Members in determining whether to purchase Timminco securities was directly influenced by the disclosure documents and statements referenced above, which incorporated the Misrepresentations.

95. Any analyst reports relied upon by the Plaintiff and other Class Members similarly relied upon material financial information containing the Misrepresentations, with the effect that any recommendation to purchase Timminco securities during the Class Period was based, in whole or in part, upon material over-statements of Timminco's financial results.

96. Therefore, as a result of the Misrepresentations, the price of Timminco's securities was artificially inflated and remained so during the Class Period.

NEGLIGENCE

97. Timminco and ~~each of~~ the Individual Timminco Defendants owed the Plaintiff and the other Class Members a duty of care, both at common law and under provisions of the Securities Act to ensure that all material information regarding the business, operations, or capital of Timminco was immediately communicated to the investing public in a truthful, complete, and accurate manner, and to immediately correct any such previously-issued material information that was no longer truthful, complete, and accurate.

98. The Photon Defendants were retained to prepare the Photon Report and make Public Oral Statements about Timminco's business and operations and they consented to the release of the Photon Report by Timminco and consented to Timminco's release of documents and Public Oral Statements that included, summarized or quoted from the Photon Report, or from Public Oral Statements made by Rogol. The Photon Defendants knew that these documents and Public Oral Statements would be relied on by investors and, as a result, they owed the Plaintiff and the other

class members a duty of care, both at common law and under provisions of the Securities Act, to ensure that all material information contained in the Photon Report and in the Public Oral Statements of Rogol was truthful, complete, and accurate, and to immediately correct any such previously-issued material information that was no longer truthful, complete, and accurate.

99. The standard of care in the circumstances required the Defendants to act fairly, honestly, candidly, openly, in accordance with the Securities Act requirements, and in the best interests of the Plaintiff and other class members.

100. For the following reasons, among others, the Defendants failed to meet the required standard of care:

(a) The Individual Timminco Defendants authorized the release of press releases, information regarding conference calls, quarterly reports, annual reports, MD&A, the Photon Report, and other public documents containing the Misrepresentations when they knew, or ought to have known, that they were false and materially misleading;

(b) The Photon Defendants made Public Oral Statements and consented to the release of the Photon Report by Timminco when they knew or ought to have known that the Photon and the Public Oral Statements were false and materially misleading;

(c) Timminco and ~~T~~the Individual Timminco Defendants failed to correct the Misrepresentations in a timely manner;

(d) Timminco and ~~T~~the Individual Timminco Defendants maintained inaccurate revenue and production forecasts that were based on the Misrepresentations; and,

(e) The Defendants failed to establish and maintain disclosure control and procedures to provide assurance that material information relating to Timminco's business and affairs was accurately and fairly presented.

101. By the actions and omissions particularized above, the Defendants violated their duty to the Plaintiff and other Class Members. The Defendants were negligent in doing so.

102. As further particularized in this Statement of Claim, it was reasonably foreseeable that the Defendants' breach of their duty would cause damage to the Plaintiff and other Class Members.

103. As further particularized in this Statement of Claim, the Plaintiff and other Class Members did suffer damage as a result of the Defendants' failure to meet their ~~duty~~ duties to the Plaintiff and other Class Members.

NEGLIGENT MISREPRESENTATION

104. ~~Timminco and the Individual~~ All of the Defendants were in a special relationship with the Plaintiff and other Class Members. ~~As a result, the~~ Timminco and the Individual Timminco Defendants owed the Plaintiff and other Class Members a duty of care in that the Timminco disclosure documents and Public Oral Statements referenced above were prepared, at least in part, with the intention they would attract the investing public to purchase Timminco securities and that they would be relied upon by the Plaintiff and other Class Members in making the decision to purchase Timminco securities.

105. The Photon Defendants owed the Plaintiff and the other class members a duty of care in that the Photon Report and Rogol's Public Oral Statements, particularized above, were prepared, at least in part, with the intention they would attract the investing public to purchase Timminco securities and that they would be relied upon by the Plaintiff and other Class Members in making the decision to purchase Timminco securities.

106. It was reasonable, and in fact expected, that the Plaintiff and other Class Members would rely on the Misrepresentations.

107. The Timminco news releases, conference calls, quarterly reports, annual reports, MD&A, and the Photon Report, as set out herein, contained the Misrepresentations, whether implicitly or explicitly, and such Misrepresentations were materially false and/or materially misleading when made.

108. ~~The~~ Timminco and the Individual Timminco Defendants made the Misrepresentations by issuing, or authorizing, permitting, and/or acquiescing in the issuance of the documents and statements referenced above. Dietrich, ~~and~~ Schimmelbusch and the ~~remaining Directors~~ other Individual Timminco Defendants made the Misrepresentations by issuing, or authorizing, permitting, and/or acquiescing in the issuance of such documents and statements, and by signing certifications for Timminco's quarterly filings that contained the Misrepresentations.

109. The Photon Defendants made the Misrepresentations in Public Oral Statements by Rogol and by consenting to the release of the Photon Report by Timminco and consenting to Timminco's release of documents and Public Oral Statements that included, summarized, or quoted from the Photon Report, or from statements made by Rogol.

110. The Defendants acted negligently in making the Misrepresentations, as particularized above. The Defendants made the Misrepresentations while knowing, while reckless in not knowing, or while they ought to have known that the Misrepresentations were false and/or materially misleading.

111. The Defendants knew or ought to have known that:

(a) by making the Misrepresentations, the price of Timminco's publicly-traded securities would be artificially inflated and remain at levels above their true value;

(b) investors would rely upon the Misrepresentations in making their decisions to purchase Timminco ~~shares~~ securities; and

(c) as a result, the Plaintiff and other Class Members would pay a higher price for the securities than their true value.

112. The Plaintiff relied upon the Misrepresentations by hearing, reading and acting upon press releases, conference calls, quarterly reports, annual reports, MD&A, and the Photon Report containing the Misrepresentations, or alternatively, by reading and acting upon documents that contained information derived from the Misrepresentations.

113. As further particularized above, the Plaintiff and other Class Members relied upon the Misrepresentations by the act of purchasing or acquiring Timminco securities on the TSX.

114. As further particularized herein, as a result of their reliance on the Misrepresentations, the Plaintiff and each other Class Members suffered damages and loss.

DAMAGES

115. During the Class Period, the Plaintiff and other Class Members purchased Timminco securities at an inflated price in reliance upon the Misrepresentations. They continued to hold the securities at an inflated price until the correction of the Misrepresentations, at which time the market adjusted the price of the securities downward to reflect the true value of Timminco shares.

116. As a result of the facts pleaded above, the Plaintiff and other Class Members have suffered damages equivalent to the loss in market value that occurred when Timminco corrected the Misrepresentations.

117. The Plaintiff and other Class Members are also entitled to recover, as damages or costs in accordance with the CPA, the costs of administering the plan to distribute the recovery in this action.

118. The Plaintiff pleads that the conduct of the Defendants was high-handed, reckless, wanton, and entirely without care, and that the Defendants were motivated by economic self-interest. Such conduct renders the Defendants liable to pay punitive damages.

VICARIOUS LIABILITY OF TIMMINCO

119. Timminco is vicariously liable for the acts and omissions of the Individual Timminco Defendants and other directors, officers, and employees of Timminco whose conduct is particularized herein.

120. All acts and omissions of Timminco were authorized, ordered, and done by the Individual Timminco Defendants and other directors, officers, and employees while in their capacity as employees or representatives of Timminco, and while engaging in the management, direction, and control of its business and operations, and as such are acts and omissions for which Timminco is vicariously liable.

PART XXIII.1 OF THE SECURITIES ACT

121. The Plaintiff intends to deliver a notice of motion seeking, among other things, an Order permitting the Plaintiff to assert the statutory causes of action particularized in Part XXIII.1 of the Securities Act, and if granted, to amend this Statement of Claim to plead these causes of action.

REAL AND SUBSTANTIAL CONNECTION TO ONTARIO

122. This action has a real and substantial connection to Ontario because, among other things:

(a) Timminco is a reporting issuer in Ontario;

(b) the shares of Timminco trade on the TSX, which is located in Toronto;

(c) the Misrepresentations and omissions were disseminated in Ontario; and,

(d) the Plaintiff resides in Ontario.

SERVICE OUTSIDE OF ONTARIO

123. This originating process may be served without court order outside Ontario in that the claim is:

(a) in respect of a tort committed in Ontario (rule 17.02(g));

(b) in respect of damages sustained in Ontario arising from a tort wherever committed (rule 17.02(h));

(c) against a person outside Ontario who is a necessary or proper party to a proceeding properly brought against another person served in Ontario (rule 17.02(o)); and,

(d) against a person carrying on business in Ontario (rule 17.02(p)).

THE RELEVANT LEGISLATION

124. The Plaintiff pleads and relies upon the *Securities Act*, the *Courts of Justice Act, supra*, and the *Class Proceedings Act, 1992, supra*, all as amended.

The Plaintiff proposes that this action be tried at the City of Toronto.

Date: May 14, 2009

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Court File No.: CV-09-378701-00CP

PENNYFEATHER
Plaintiff

- and -

TIMMINCO LIMITED, *et al.*
Defendants

ONTARIO
SUPERIOR COURT OF JUSTICE

Proceeding commenced at Toronto
Proceeding under the *Class Proceeding Act, 1992*

AMENDED STATEMENT OF CLAIM

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RE TIMMINCO LIMITED et al.
Applicant

Court File No. CV-12-9539-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(Commercial List)

Proceeding commenced at Toronto

BOOK OF AUTHORITIES
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